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SHAREHOLDER PROPOSAL DEVELOPMENTS DURING THE 2015 PROXY SEASON

To Our Clients and Friends:

This client alert provides an overview of shareholder proposals submitted to public companies for 2015 shareholder meetings, including statistics, notable decisions from the staff (the "Staff") of the Securities and Exchange Commission (the "SEC") on no-action requests,[1] and information about litigation regarding shareholder proposals.[2]

I. Shareholder Proposal Statistics and Voting Results

A. Shareholder Proposals Submitted

According to data from Institutional Shareholder Services ("ISS"), shareholders have submitted approximately 943 proposals for 2015 shareholder meetings, which surpasses the total of 901 proposals submitted as of a comparable time last year. For 2015, across four broad categories of shareholder proposals--governance and shareholder rights; environmental and social issues; executive compensation; and corporate civic engagement (which includes proposals regarding contributions to or membership in political, lobbying, or charitable organizations)--the most frequently submitted proposals were governance and shareholder rights proposals (with approximately 352 submitted), largely due to the unprecedented number of proxy access proposals (108 proposals). If not for the dramatic rise in the number of proxy access proposals, proposals on environmental and social issues would have again comprised the largest category of proposals (with approximately 324 submitted), continuing a trend that began in 2014.

The most common 2015 shareholder proposal topics, along with the approximate numbers of proposals submitted, were:

- political and lobbying activities (110 proposals),
- proxy access (108 proposals), and
- independent chair (76 proposals).

By way of comparison, the most common 2014 shareholder proposal topics were:

- political and lobbying activities (126 proposals),
- independent chair (68 proposals), and
- climate change (56 proposals).

As is typically the case, John Chevedden and shareholders associated with him submitted by far the highest number of shareholder proposals for 2015 shareholder meetings. However, the season saw a dramatic increase in the number of proposals submitted by the New York City Comptroller, which submitted or co-filed at least 86 proposals on behalf of five New York City pension funds, including 75 proxy access proposals, as part of the Comptroller's "Boardroom Accountability Project." Other proponents that were reported to have submitted or co-filed at least 20 proposals each included: Calvert Asset Management Co. (40, largely focused on environmental matters); the New York State Common Retirement Fund (40, largely focused on environmental and political matters); AFL-CIO (36, largely focused on executive compensation matters); As You Sow Foundation (32, largely focused on environmental matters); Trillium Asset Management LLC (25, largely focused on environmental and social matters); Walden Asset Management (25, largely focused on environmental, social, and political matters); and UNITE HERE (22, largely focused on governance and shareholder rights matters).

Shareholder proponents withdrew approximately 17% of the proposals submitted for 2015 shareholder meetings, a decrease as compared to approximately 19% of the proposals submitted for 2014 meetings and approximately 28% of proposals submitted for 2013 meetings.

B. Shareholder Proposal No-Action Requests

During the 2015 proxy season, companies submitted 318 no-action requests to the Staff as compared to approximately 295 in the 2014 proxy season. In 2015, the percentage of no-action letters that were denied by the Staff jumped significantly to 39%, the highest level in four years.

The following table summarizes the responses to no-action requests that the Staff issued during the 2015 and 2014 proxy seasons:

	2015	**2014**
Total no-action requests submitted	318[3]	295
Total Staff responses issued[4]	268	286
No-action requests withdrawn	55	60
Responses granting or denying exclusion	213	226
Exclusions granted	130 (61%)	161 (71%)
Exclusions denied	83 (39%)	65 (29%)
No-action requests for which Staff did not issue a response due to review of Rule 14a-8(i)(9) interpretations	48	N/A

Based on a review of the no-action requests, the Staff concurred that shareholder proposals could be excluded for the following principal reasons:

- 35% based on procedural arguments, such as timeliness or defects in the proponent's proof of ownership;
- 32% based on ordinary business arguments;
- 21% because the company had substantially implemented the proposal; and
- 2% because the proposal was vague or false and misleading.[5]

Two aspects of the foregoing data are worth noting. The first is the sharp drop in exclusions of proposals for being vague or false and misleading under Rule 14a-8(i)(3). In 2014, by contrast, Rule 14a-8(i)(3) accounted for 18% of excluded proposals, and only exclusions based on procedural arguments constituted a more frequent basis for exclusion. The second is that the Staff declined to issue responses to 48 no-action requests, or 15% of the 318 no-action requests submitted, in light of the Staff's announcement on January 16, 2015 that it would no longer express views on Rule 14a-8(i)(9) during the 2015 proxy season (discussed further below in Section II.A). Rule 14a-8(i)(9), which provides for the exclusion of a shareholder proposal that conflicts with a company proposal to be submitted for a vote at the same shareholder meeting, had accounted for 11% of the exclusions granted by the Staff during the 2014 proxy season.

Of the shareholder proposals for which no-action relief was denied, 58% were challenged as being either vague or false and misleading under Rule 14a-8(i)(3), making these arguments the most frequently rejected arguments, as they were during the 2014 proxy season. Other frequently unsuccessful arguments included that the company had substantially implemented the proposal (28% of denials), that the proposal related to the company's ordinary business operations (24% of denials), and that there was a procedural defect in the submission of the proposal (14% of denials).[6]

C. Shareholder Proposal Voting Results

1. Overview

Most shareholder proposals voted on in 2015 did not receive majority support. Based on the 447 shareholder proposals for which ISS provided voting results for 2015 meetings,[7] proposals averaged support of 33.2% of votes cast. Six proposal topics that received high shareholder support, including four that averaged majority support, were:

- Adoption of majority voting in uncontested director elections, averaging 76.6% of votes cast, compared to 57.2% in 2014;
- Board declassification, averaging 72.6% of votes cast, compared to 84.0% in 2014;
- Proxy access, averaging 54.6% of votes cast, compared to 35.3% in 2014;

- Elimination of supermajority vote requirements, averaging 53.0% of votes cast, compared to 69.6% in 2014;
- Shareholder ability to call special meetings, averaging 44.4% of votes cast, compared to 41.6% in 2014; and
- Written consent, averaging 39.4% of votes cast, compared to 38.5% in 2014.

Primarily as a result of the success of proxy access proposals, 16.7% of proposals (75 proposals) voted on at 2015 shareholder meetings received support from a majority of votes cast, compared to 14.8% of proposals (64 proposals) in 2014. The table below shows the principal topics addressed in proposals that received a majority of votes cast at a number of companies:

	2015 Majority Votes	**2014 Majority Votes**
Proxy access	38[8]	5
Majority voting in uncontested director elections	7	15
Board declassification	6	14
Elimination of supermajority vote requirements	6	9
Shareholders' ability to call special meetings	4	4
Independent chair	2	4
Shareholder approval of shareholder rights plan	2	4
Shareholders' ability to act by written consent	2	0
Submit severance agreements to shareholder vote	2	1
No accelerated vesting of equity awards upon a change of control	1	4
Political and lobbying activities	0	3

2. Political Contributions and Lobbying Proposals

Although political contributions and lobbying proposals again were frequent shareholder proposal topics, the total number of such proposals decreased, with shareholders submitting 110 such proposals for 2015 shareholder meetings, compared to 126 proposals for 2014 shareholder meetings. As in prior years, these proposals generally request more robust disclosure of company political spending and lobbying activities. Political spending or lobbying proposals averaged support of 28.8% of votes cast

and none received majority support during 2015, although three such proposals received majority support in 2014.

3. Climate Change Proposals

Climate change remains a frequent shareholder proposal topic--and indeed, the most prevalent of the environmental proposals submitted for 2015 shareholder meetings. However, the total number of such proposals decreased slightly, with shareholders submitting 50 climate change proposals for 2015 shareholder meetings, down from 56 proposals in 2014. Climate change proposals in 2015, as in prior years, continued to primarily focus on greenhouse gas emissions goals and accounting, reports on greenhouse gas emissions reductions targets, and disclosure of the company's exposure to risks relating to climate change. Climate change proposals averaged support of 23.5% votes cast. As in 2014, none received majority support during 2015.

4. Executive Compensation Proposals

Consistent with prior years, proposals touching on executive compensation matters were a recurrent topic in 2015, with approximately 131 proposals submitted. The most frequent proponents were John Chevedden and the AFL-CIO. The 66 proposals voted on averaged support of 26.7% of votes cast. In 2015, three proposals--a proposal seeking to limit accelerated vesting of equity awards submitted to FirstMerit Corp. and proposals requesting that severance agreements be subject to a shareholder vote submitted to Hologic, Inc. and TCF Financial Corp.--have received a majority of votes cast. The most frequent executive compensation shareholder proposals were:

- Proposals seeking to limit accelerated vesting of equity awards (34), with the 23 proposals voted on averaging support of 32.4% of votes cast;
- Proposals seeking adoption or disclosure of clawback policies (22), with the 13 proposals voted on averaging support of 30.3% of votes cast; and
- Proposals seeking reports on the ratio between the compensation paid to the chief executive officer and the median employee (15); the Staff concurred that three of these proposals were excludable on the basis of Rule 14a-8(i)(7), and subsequently, the remaining proposals were withdrawn.

II. 2015 Rule 14a-8 Developments

The 2015 proxy season was an exceptional season: the Staff stated that, pending an internal review, it would no longer express views during the 2015 proxy season on the availability of Rule 14a-8(i)(9), reversed its position mid-season on whether an independent chair proposal was vague and misleading under Rule 14a-8(i)(3), and issued a number of interpretations that appeared inconsistent with precedent.

A. Rule 14a-8(i)(9) Review

1. Background

Pursuant to Rule 14a-8(i)(9), a company may exclude a shareholder proposal if the proposal "directly conflicts with one of the company's own proposals to be submitted to shareholders at the same meeting." Rule 14a-8(i)(9) stems from a 1967 amendment to Rule 14a-8(a), whereby the SEC clarified that companies could exclude from their proxy materials shareholder proposals that were "counter proposals to matters to be submitted by the management."[9] Since the adoption of this exclusion in 1967, the Staff consistently has permitted companies to exclude a shareholder proposal where the proxy statement also contained a conflicting company proposal. The rationale behind the exclusion is that inclusion in the proxy statement of a shareholder proposal that conflicts with a company proposal "would present alternative and conflicting decisions for shareholders and would create the potential for inconsistent and ambiguous results."[10]

Fifty-two companies that received shareholder proposals for 2015 meetings filed no-action requests to exclude a shareholder proposal under Rule 14a-8(i)(9). Most of the proposals challenged under Rule 14a-8(i)(9) pertained either to the adoption of proxy access (26) or the reduction of the ownership threshold required in order for shareholders to call a special meeting (12). Other challenged proposals included the adoption of a clawback policy (4), the prohibition of accelerated vesting of equity awards upon a change in control (4), the elimination of supermajority voting provisions (3), the adoption of quantifiable metrics for equity compensation plans (2), and opting out of a state's unsolicited takeover act (1).

2. January 2015 Announcement

In October 2014, Whole Foods Market, Inc. became the first company to seek to exclude a proxy access shareholder proposal under Rule 14a-8(i)(9). The challenged proposal requested that the company adopt a proxy access provision pursuant to which a shareholder or group of shareholders could nominate and include in the company's proxy materials up to 20% of the company's directors, subject to a 3%/3-year ownership threshold. Whole Foods' conflicting proxy access proposal had a significantly more restrictive ownership provision (9%/5-year threshold to be satisfied by a single shareholder) and allowed for nominations only up to 10% of the company's directors. In December 2014, the Staff concurred that Whole Foods could exclude the proxy access shareholder proposal under Rule 14a-8(i)(9). That decision provoked a backlash among public pension funds, reflected in a letter from the Council of Institutional Investors criticizing the Staff's interpretation as "overly broad and inconsistent with the purpose of" Rule 14a-8(i)(9).[11]

In January 2015, SEC Chair Mary Jo White announced that she was directing the Staff to review Rule 14a-8(i)(9) and report to the SEC on its review. Concurrently with this announcement, the Staff announced that pending its review, it would no longer express a view during the 2015 proxy season on the availability of Rule 14a-8(i)(9).[12] The Staff then reversed the Whole Foods no-action letter and two no-action letters allowing exclusion of proposals seeking to reduce the ownership threshold required in order for shareholders to call a special meeting. The Staff also notified each company with

a pending Rule 14a-8(i)(9) no-action request on any shareholder proposal that it would not express a view on the company's ability to exclude the proposal under that rule. In connection with the Staff's review of Rule 14a-8(i)(9), in February 2015 ISS announced that it would consider the exclusion of a shareholder proposal a "governance failure" that could result in ISS recommending votes "against" company directors, unless the company had obtained voluntary withdrawal of the proposal by the proponent, or had received no-action relief from the SEC or a U.S. District Court ruling allowing for exclusion of the proposal. ISS noted that the inclusion of a management-sponsored proposal in a company's proxy statement in place of a conflicting shareholder proposal would not affect its negative vote recommendation against company directors.

3. Company Responses

The companies that submitted no-action request letters under Rule 14a-8(i)(9) have varied in their responses to the Staff's decision not to express views with respect to the rule's availability. One company, Deere & Co., had already obtained no-action relief under Rule 14a-8(i)(9) and filed its proxy statement prior to the Whole Foods reversal, and was therefore unaffected by the reversal. As of June 20, 2015, of the other 47 companies that challenged a proposal solely on the grounds of Rule 14a-8(i)(9):

- twenty-two companies (47%) included the shareholder proposal in the company's proxy materials and recommended that shareholders vote "against" it;
- ten companies (21%) included in the company's proxy materials both the shareholder proposal and a conflicting company proposal;
- six companies (13%) procured the withdrawal of the shareholder proposal;
- four companies (9%) adopted measures conflicting with those called for in the proposal and included the shareholder proposal in the company's proxy materials and recommended that shareholders vote "against" it;
- four companies (9%) supported the shareholder proposal; and
- one company[13] has not yet filed a proxy statement.

4. Status of SEC Review

Chair White gave a speech in March in which she reflected on her philosophical approach to the review of Rule 14a-8(i)(9). While noting the "not insignificant consternation" regarding the decision not to express views with respect to the availability of Rule 14a-8(i)(9) and expressing her understanding of the frustration of companies that had anticipated relying on the rule, Chair White stated that her directive "was driven by a deeper concern that the application of (i)(9), as originally interpreted by the [S]taff, could result in unintended consequences and potential misuse of our process. The purpose of the review is to think carefully about the application of the rule and a variety

of related questions."[14] According to Chair White and Keith Higgins, Director of the Division of Corporation Finance, such related questions include:

- Is a shareholder proposal automatically conflicting if the company makes a proposal in response to it?
- Are the shareholder and company proposals conflicting if they have the same subject matter but different terms?
- What if the company proposal purports to provide a right to shareholders but sets forth conditions that no shareholder meets?
- If the company excludes a shareholder proposal as conflicting, should the company be required to disclose the existence of the shareholder proposal?
- Should the company have to disclose its *motivations for its own proposal?*

Comment letters that have been submitted in connection with the Staff's review of its application of Rule 14a-8(i)(9) are available at http://www.sec.gov/comments/i9review/i9review.shtml. While there is no public deadline for the Staff's review, the Staff has informally indicated that its objective is to issue its report before the 2016 proxy season. However, depending on the nature of its report and any recommendations, it is not certain whether the Staff will again be in a position to address Rule 14a-8(i)(9) no-action letters during the 2016 proxy season.

B. Proxy Access Proposals

1. Background

"Proxy access" refers to providing shareholders the ability to include in a company's proxy statement and on the company's proxy card one or more shareholder-nominated candidates for election to the company's board of directors. Proxy access provides shareholders an alternative to the traditional process of running an election contest to elect a dissident slate of directors to a company's board, both eliminating the expense of printing and mailing a proxy statement soliciting voting authority for the shareholder's director candidates, and eliminating the difficult process of having competing proxy cards. Proxy access therefore significantly reduces the costs and procedural difficulties of running a proxy contest.

Between 2011, when a federal appeals court struck down an SEC rule (Rule 14a-11) requiring universal proxy access at U.S. public companies, and 2014, only 10 companies adopted proxy access rights. Many of these companies had faced various corporate governance challenges after which shareholders submitted a non-binding proposal asking the company to adopt *proxy access*.

Proxy access shareholder proposals were first voted on at 2012 annual meetings, and 46 such proposals had been voted on by the end of 2014. Twenty-two of these proposals included the 3%/three-year ownership requirements from vacated Rule 14a-11. State pension funds primarily submitted these

proxy access proposals and initially targeted companies with well-known corporate governance challenges. The other 24 proxy access shareholder proposals requested that proxy access be available to shareholders satisfying lower ownership requirements (*e.g.*, 1% for at least one year). The voting results for these proposals are shown in the following table:

Proxy Access Shareholder Proposals Voted On: 2012 – 2014			
Ownership Threshold	# of Proposals Voted On	# of Proposals Passed	Average Vote
3%/three years	22	10	45.6%
2%/one year	1	0	21.0%
1% or less	23	0	20.2%

2. Proxy Access Proposals in 2015

The proxy access movement was catalyzed in 2015, when the New York City Comptroller and other shareholders submitted 108 proxy access shareholder proposals. The Comptroller's proposal requests that the company's board adopt and present for shareholder approval a bylaw that would require the company to include in its proxy materials the names of director candidates nominated by a shareholder (or group of shareholders) that has beneficially owned at least 3% of the company's outstanding stock continuously for at least three years. The proposals, which are non-binding, ask that the number of proxy access nominees not exceed 25% of the board.[15]

The Comptroller's "Boardroom Accountability Project" targeted companies based on three issues of concern: carbon-intensive coal, oil, gas, and utility companies; companies lacking board diversity; and companies with failed or low "say-on-pay" votes in 2014. The Comptroller noted that by submitting its proposals it was "seeking to change the market by having more meaningful director elections through proxy access, which will make boards more responsive to shareowners."

In the wake of the Staff's decision not to express views with respect to the availability of Rule 14a-8(i)(9), company responses to these shareholder proposals have varied, as reflected in the following table as of June 20, 2015:

Actions in Response to Proxy Access Shareholder Proposals	**Number of Companies**
Included the Shareholder Proposal in the Proxy Statement	*85*
Recommended votes "against" the shareholder proposal without any further action[16]	66
Preemptively adopted a proxy access bylaw amendment and	9

Actions in Response to Proxy Access Shareholder Proposals	Number of Companies
recommended votes "against" the shareholder proposal	
Recommended votes "against" the shareholder proposal and included a binding or advisory company-sponsored proposal to approve proxy access on different terms	7
Recommended votes "for" the shareholder proposal	2
Declined to make a recommendation as to how shareholders should vote	1
Excluded the Shareholder Proposal from its Proxy Statement and Either Adopted or Agreed to Adopt Proxy Access, or Agreed to Include a Binding, Company-Sponsored Proposal, with Terms Similar to the Shareholder Proposal	*13*
Excluded the Shareholder Proposal after Obtaining No-Action Relief on Procedural Grounds	*2*
Not Yet Known	*8*

3. Annual Meeting Results

Proxy access shareholder proposals have received a majority of votes cast at 48 of the 82 companies that have held such a vote in 2015 as of the date of this client alert, averaging support of 54.6% of votes cast. This includes:

- Eight companies[18] that have held a vote on a proxy access shareholder proposal after preemptively adopting proxy access with a higher ownership threshold, a more restrictive limit on the number of nominees, and/or a more restrictive limit on the size of the nominating group. The shareholder proposal was approved at four of these eight companies, with support averaging 50.2% of votes cast.

- Seven companies[19] that have held votes on both a proxy access shareholder proposal and a conflicting, company-sponsored proxy access proposal. The shareholder proposal was approved at three of these seven companies, with support averaging 55.4% of votes cast, and at one company neither the company-sponsored proposal nor the shareholder proposal received a majority vote.[20]

ISS has recommended a vote in favor of every proxy access shareholder proposal voted on thus far during 2015, even in instances where the company has preemptively adopted proxy access or sought shareholder approval of a company-sponsored proposal with more restrictive terms.

C. "Materially False or Misleading" Argument Developments

Rule 14a-8(i)(3) permits the exclusion of a shareholder proposal that is "contrary to any of the Commission's proxy rules, including Rule 14a-9, which prohibits materially false or misleading statements in proxy soliciting materials." As discussed earlier, company assertions in no-action requests that shareholder proposals were either vague or false and misleading and therefore excludable under Rule 14a-8(i)(3) were the most frequently rejected arguments during both the 2015 and 2014 proxy seasons, but the number of proposals for which those arguments succeeded dropped significantly in 2015.

1. Standard for Determining Materiality

As discussed in our client alert entitled Shareholder Proposals Developments During the 2014 Proxy Season, last year the U.S. District Court for the Eastern District of Missouri granted a declaratory judgment in *Express Scripts Co. v. Chevedden**[21]*** in favor of the company, ruling that the proposal contained materially false and misleading statements, pursuant to Rule 14a-8(i)(3). When reaching its decision, the court stated:

> [W]hen viewed in the context of soliciting votes in favor of a proposed corporate governance measure, statements in the proxy materials regarding the company's existing corporate governance practices are important to the stockholder's decision whether to vote in favor of the proposed measure. . . . As such, the Court finds these misstatements are material and, therefore, not in compliance with SEC rules and regulations.

A decade before *Express Scripts*, the Staff announced that it would change its application of Rule 14a-8(i)(3), stating in Staff Legal Bulletin No. 14B (Sept. 15, 2004) ("SLB 14B") that going forward "exclusion or modification under rule 14a-8(i)(3)" would be "appropriate" only in limited situations, such as where the company "demonstrates objectively that a factual statement is materially false or misleading." The Staff has viewed few statements as satisfying this standard.[22] The *Express Scripts* decision thus created an opportunity for the Staff to readdress its historically narrow interpretation of Rule 14a-8(i)(3).

In 2015, the Staff granted a no-action letter to Ferro Corporation concurring that a shareholder proposal received from Kenneth Steiner and John Chevedden was excludable under Rule 14a-8(i)(3) as false and misleading.[23] The proposal requested that Ferro, which is incorporated in the State of Ohio, reincorporate in the State of Delaware, and the supporting statements made several representations about Ohio corporate law that the company argued to were materially false and misleading under the objective criteria laid out in SLB 14B. The Staff concluded that Ferro "demonstrated objectively that certain factual statements in the supporting statement are materially

false and misleading such that the proposal as a whole is materially false and misleading."[24] With the exception of Ferro, the Staff rejected all other arguments based on materially false or misleading statements pursuant to Rule 14a-8(i)(3) this season, including an AT&T Inc. no-action request that cited *Express Scripts*.[25] In discussing its application of Rule 14a-8(i)(3), the Staff has focused not only on whether a statement is objectively false, but whether it is material to the proposal. Despite the court's conclusion in *Express Scripts* that in the context of corporate governance proposals, a shareholder's "statements … regarding the company's existing corporate governance practices are important to the stockholder's decision whether to vote in favor of the proposed measure," it appears that the Staff continues to apply a stricter approach to assessing materiality than *Express Scripts*.

2. "Vague and Indefinite" Arguments

Rule 14a-8(i)(3) also permits the exclusion of a shareholder proposal that is so vague and indefinite as to be misleading. In 2015, the Staff reversed its position mid-season on whether specific language in a line of independent chair proposals was vague and misleading under Rule 14a-8(i)(3). In December 2014, Pfizer submitted a no action request letter arguing that the company could exclude an independent chair proposal submitted by John Chevedden and Kenneth Steiner under Rule 14a-8(i)(3) because it was vague and indefinite in the context of Pfizer's facts. Specifically, Pfizer argued that the proposal's attempt to define an independent director as someone whose directorship constitutes his or her "only nontrivial professional, familial or financial connection to the company or its CEO" was vague because Pfizer's non-employee directors are subject to stock ownership guidelines, which ensure that there is a nontrivial financial connection between directors and Pfizer. The company pointed to *Abbott Laboratories* (avail. Jan. 13, 2014) in which the Staff concurred that the company could exclude an independent lead director proposal on the grounds that it was vague and indefinite where the standard of independence would have been "a person whose directorship constitutes his or her only connection to [the] company."[26] On December 22, 2014, the Staff concurred that Pfizer could exclude the shareholder proposal under Rule 14a-8(i)(3) on the grounds that it was vague and indefinite.

Many companies that had received substantially similar proposals to Pfizer had not challenged these proposals due to the differences in the language between the Pfizer and Abbott proposals. Following the Staff's decision in *Pfizer*, a number of these companies filed similar no-action requests. However, beginning in late February 2015, 66 days after the Staff had issued the *Pfizer* decision, the Staff denied those no-action requests, reversing the position the Staff took in *Pfizer*. The Staff's responses stated: "Although the staff has previously agreed that there is some basis for your view, upon further reflection, we are unable to conclude that the proposal, taken as a whole, is so vague or indefinite that it is rendered materially misleading."[27]

Similarly, the Staff rejected a vagueness argument on a proposal submitted to Bank of America, notwithstanding that the proposal was only slightly revised from a proposal that the Staff had previously concurred was excludable under Rule 14a-8(i)(3). In Staff Legal Bulletin No. 14B (Sept. 15, 2004), the Staff stated that a shareholder proposal is excludable under Rule 14a-8(i)(3) as vague and indefinite if "neither the stockholders voting on the proposal, nor the company in implementing the proposal (if adopted), would be able to determine with any reasonable certainty exactly what actions or

measures the proposal requires." Discussing this standard in Staff Legal Bulletin No. 14G (Oct. 16, 2012), the Staff stated, "In evaluating whether a proposal may be excluded on this basis, we consider only the information contained in the proposal and supporting statement and determine whether, based on that information, shareholders and the company can determine what actions the proposal seeks." In January 2015, Bank of America submitted a no-action request arguing that the company could exclude a proposal submitted by Bartlett Naylor under Rule 14a-8(i)(3) because it was vague and indefinite, among other reasons. The proposal requested that the board create a "stockholder value committee" to explore a plan for divesting all "non-core banking business segments." The 2015 proposal was a slightly revised version of a proposal Mr. Naylor submitted the previous year, which the Staff had concurred could be excluded under Rule 14a-8(i)(3).[28] The proposal did not define "non-core banking business segments," but instead defined "non-core banking operations" as "operations that are conducted by affiliates other than the affiliate the corporation identifies as Bank of America, N.A. which holds the FDIC Certificate No 3510." Bank of America argued that the 2015 proposal, as with the proposal received in the prior year, failed to adequately define "non-core banking business segments," and that shareholders could not know from the face of the proposal what operations were included or excluded from the action requested. Nevertheless, in a March 2015 letter, the Staff stated that it was unable to concur with the company's exclusion of the proposal.

D. Developments in the Ordinary Business Exception

Rule 14a-8(i)(7) permits a company to omit from its proxy materials a shareholder proposal that relates to the company's "ordinary business" operations, except that a proposal may be able to avoid exclusion under this provision if it, among other things, focuses on a "significant policy issue," and has sufficient nexus to the company. Although the application of Rule 14a-8(i)(7) in the context of a specific shareholder proposal was the subject of litigation during 2015, which is discussed in Section III below, the Staff continued to address no-action requests that were based on Rule 14a-8(i)(7) during the 2015 proxy season. The Staff did not recognize any new significant policy issues during the season, but addressed the applicability of that exception in the context of new proposals.

1. Pharmaceutical Pricing Proposals

This season saw the return of a shareholder proposal campaign targeting how pharmaceutical companies determine the price of their products. The UAW Retiree Medical Benefits Trust ("UAW") targeted six pharmaceutical companies with proposals requesting that the companies prepare reports "on the risks to [the companies] from rising pressure to contain U.S. specialty drug prices." The proposals defined specialty drugs as "those that cost more than $600 per month" and requested that the reports address specific matters, including the companies' responses to risks as a result of price disparities between countries, price sensitivity of specific stakeholders, and the use of cost-effectiveness studies by pharmaceutical purchasers. The supporting statements to the proposals included specific references to at least one of the applicable companies' specialty drugs as well as references to media publications discussing the costs associated with the products. According to specialty news sources, three of the six companies made agreements with the UAW related to implementing at least some aspects of the proposals.[29]

Three companies sought no-action letters from the Staff arguing that the proposals could be excluded under the ordinary business exceptions in Rule 14a-8(i)(7). The companies' main argument to the Staff was that the proposals related to the pricing of their pharmaceutical products and thus were excludable as relating to the ordinary businesses of the companies because setting the prices for products is a decision for management, not shareholders. The companies also included additional Rule 14a-8(i)(7) arguments including that the proposals sought to micro-manage the companies, that the proposals related to public policy concerns only tangentially, and that even if the proposals related to significant policy issues they were excludable because they also involved matters that are fundamental to ordinary business, specifically, product pricing. The Staff rejected the no-action requests, in each case stating that the applicable proposal focused on "fundamental business strategy with respect to its pricing policies for pharmaceutical products" and thus the proposals were not excludable pursuant to Rule 14a-8(i)(7).[30] Over a decade ago, the Staff used very similar language to reject the no-action requests submitted by Bristol Myers Squibb Co. and Eli Lilly and Co.[31] In *Bristol-Myers Squibb Co.* and *Eli Lilly and Co.* the proponents requested that the companies adopt "a policy of price restraint" with the *Bristol-Myers Squibb Co.* proposal specifying that the policy would apply to "pharmaceutical products for individual consumers and institutional purchasers." The *Bristol-Myers Squibb Co.* proposal also requested that the company report to shareholders "on changes in policies and pricing procedures for pharmaceutical products." Although the *Bristol-Myers Squibb Co.* and *Eli Lilly and Co.* proposals were arguably more restrictive than the proposals recently submitted by the UAW because they required the companies to adopt specific pricing policies instead of preparing reports about pricing risks, in all cases the Staff has found that the "pricing policies for pharmaceutical products" are part of companies' "fundamental business strateg[ies]" and are thus not excludable from proxy statements pursuant to Rule 14a-8(i)(7). Each company included the applicable proposal in their proxy materials and the proposals failed to gain majority support.

2. Political Speech Proposals

In 2015, the National Center for Public Policy Research ("NCPPR") submitted a number of proposals regarding the protection of political free speech rights of company employees. The NCPPR's early proposals requested that companies adopt anti-discrimination policies protecting employees' rights to engage in the political process without retaliation. The Staff concurred in the exclusion of these proposals under Rule 14a-8(i)(7), as relating to companies' ordinary business operations.[32] Some companies instead obtained withdrawal of the proposals by satisfying the proponent that its concerns were addressed through existing policies or by revising policies in response to a proposal.[33] NCPPR revised its proposals mid-season, requesting that companies review their human rights policies and report on any areas in which additional policies might be needed to protect human rights more generally, including, at management's discretion, policies related to participation in government without retribution. The Staff continued to concur in the exclusion of such proposals under Rule 14a-8(i)(7), despite the change in phrasing.[34] Thus, these no-action letters help to demonstrate that merely labeling a proposal as implicating non-discrimination or human rights issues is not sufficient to avoid evaluation of whether a proposal seeks to address ordinary business operations.

III. Shareholder Proposal Litigation

On April 14, 2015, a three-judge panel of the U.S. Court of Appeals for the Third Circuit unanimously ruled that a shareholder proposal submitted to Wal-Mart was excludable under Rule 14a-8,[35] reversing a December 2014 judgment by the U.S. District Court for the District of Delaware.[36] The Third Circuit announced its ruling on an expedited basis in light of Wal-Mart's proxy printing deadline and stated that it would issue an opinion explaining the rationale for its ruling at a later time. On July 6, 2015, the Third Circuit issued its opinion.[37]

The shareholder proposal was submitted by Trinity Wall Street ("Trinity"), a religious organization, for consideration at Wal-Mart's 2014 annual meeting. The proposal sought to amend Wal-Mart's Compensation, Nominating and Governance Committee's charter to provide for "oversight" concerning the "formulation and implementation" of "policies and standards that determine whether or not the Company should sell" certain products.[38] The proposal's supporting statement stated that under the proposal the Committee's role would include determining whether to sell "guns equipped with magazines holding more than ten rounds of ammunition."[39]

Under the SEC's proxy rules, a company may exclude from its proxy materials pursuant to Rule 14a-8(i)(7) shareholder proposals relating to the company's ordinary business operations. Wal-Mart obtained, in March 2014, a no-action letter from the Staff, which concurred that the proposal was excludable under Rule 14a-8(i)(7) because it related to products sold by Wal-Mart. Trinity then filed suit in federal district court in April 2014 seeking to enjoin Wal-Mart from distributing its 2014 proxy materials without including Trinity's proposal. The District Court denied Trinity's motion for a preliminary injunction, finding that Trinity failed to establish a likelihood of success on the merits of its claim that the proposal was not excludable under Rule 14a-8(i)(7) given the proposal's focus on the products Wal-Mart sells. After Wal-Mart distributed its 2014 proxy materials, Trinity amended its complaint to seek declaratory relief as to the omission of its proposal from the 2014 proxy materials, as well as prospective relief based on Trinity's intent to resubmit the proposal for 2015. Both Wal-Mart and Trinity subsequently sought summary judgment. In addition to arguing that the proposal was excludable under Rule 14a-8(i)(7), Wal-Mart also argued that the proposal was excludable under Rule 14a-8(i)(3) because, given the "subjectivity and ambiguity of key terms in the [p]roposal" such as "values" and "family or community," it was so vague and indefinite that "neither the [shareholders] voting on the proposal, nor the company in implementing the proposal (if adopted), would be able to determine with any reasonable certainty exactly what actions or measures the proposal requires."[40]

Following oral argument, on November 26, 2014, the District Court ruled in Trinity's favor, holding that the proposal was not excludable under either Rule 14a-8(i)(7) or Rule 14a-8(i)(3) and enjoining Wal-Mart from distributing its 2015 proxy materials without including Trinity's proposal. Although Wal-Mart argued that Trinity's proposal related to the products it sells, the District Court held that the proposal was "best viewed as dealing with matters that are not related to Wal-Mart's ordinary business operations." The District Court reasoned that the proposal does not dictate to management, but instead "seeks to have Wal-Mart's *Board* oversee the development and effectuation of a Wal-Mart policy."[41]

Wal-Mart appealed the District Court's decision, arguing that it contradicted prior SEC rulemaking and would "leave the Rule 14a-8(i)(7) ordinary business exclusion in tatters" by creating "what amounts to a board action exception to Rule 14a-8(i)(7), notwithstanding the SEC's plain guidance that no such exception exists."[42] In addition, Wal-Mart argued that the proposal was excludable under Rule 14a-8(i)(3) as vague and indefinite because key terms were undefined, subjective, and ambiguous. The appeal attracted numerous amicus briefs on both sides, including briefs from major corporate trade associations on behalf of Wal-Mart and a group of law professors and anti-gun activists on behalf of Trinity. On April 14, 2015, only six days after oral argument, the Third Circuit reversed the District Court's decision. Wal-Mart subsequently distributed its 2015 proxy materials without including Trinity's proposal.

These proceedings generated substantial debate on a number of important issues, including the scope of the "ordinary business" exclusion under Rule 14a-8(i)(7). The Third Circuit panel unanimously agreed that the proposal was excludable under Rule 14a-8(i)(7), although a concurring opinion applied a different analysis than the majority opinion, and two of the judges also concluded that the proposal was excludable under Rule 14a-8(i)(3) as being vague and indefinite. The proceedings demonstrate that shareholders may use litigation as an alternative to the Staff no-action letter process.

Conclusion

- The developments discussed above demonstrate the continued complexity of the shareholder proposal process, particularly when litigation is involved. Some lessons that companies should keep in mind as they begin to look toward 2016 include:

- Uncertainty of the Future of Rule 14a-8(i)(9): The Staff has released very limited information regarding its ongoing review of its application of Rule 14a-8(i)(9). It is unclear how the Staff's review will affect application of the rule, and given the politics at the SEC, it is uncertain whether Rule 14a-8(i)(9) will again be available before the 2016 proxy season.

- Proxy Access: With the success of the 2015 shareholder campaign, proxy access will likely remain a top shareholder proposal topic. Companies that did not receive a proxy access shareholder proposal in 2015 should begin considering how to respond to a possible proxy access shareholder proposal in 2016.

- Staff Unpredictability: The Staff demonstrated in the 2015 proxy season with proxy access and independent chair shareholder proposals that it is willing to reverse its positions "upon further reflection" on the topic, despite the potentially disruptive effect that doing so might have on companies in the midst of proxy season.

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[1] Gibson, Dunn & Crutcher LLP assisted companies in submitting the shareholder proposal no-action requests discussed in this alert that are marked with an asterisk (*).

[2] For the purposes of reporting statistics regarding no-action requests in this alert, references to the "2015 proxy season" refer to the period between October 1, 2014 and May 31, 2015. Where statistics are provided for prior years, the data is for a comparable period in those years. All data in this alert on shareholder proposals submitted, withdrawn, and voted on comes from ISS publications and the ISS shareholder proposals database, and includes proposals submitted at any time prior to June 1, 2015 for meetings held at any time in 2015, unless otherwise noted. Voting results are reported on a votes cast basis (votes for or against) and do not address the impact of abstentions. Other data was derived from no-action letters posted on the SEC's website.

[3] From October 1, 2014 through May 31, 2015, the Staff had responded (or declined to issue a response due to the review of Rule 14a-8(i)(9)) to 316 of the 318 no-action requests submitted.

[4] Includes Staff-issued responses in order to either grant or deny exclusion of a proposal, or following withdrawal of a no-action request, usually in response to a proponent's withdrawal of a proposal.

[5] The remaining 10% of the proposals that were excluded were excluded on other bases under Rule 14a-8.

[6] The total exceeds 100% because many no-action requests assert more than one argument for exclusion.

[7] As a matter of practice, the vast majority of shareholder proposals submitted to companies for annual meetings are submitted under Rule 14a-8 rather than pursuant to companies' advance notice bylaws. However, because the ISS data does not indicate whether a shareholder proposal has been submitted under Rule 14a-8 or under a company's advance notice bylaws, it is possible that the ISS data includes voting results for shareholder proposals not submitted pursuant to Rule 14a-8. This discrepancy is likely to account for only a very small number of proposals.

[8] Note that the information provided in this table, consistent with the other ISS data in this client alert, is as of June 1, 2015. In Section II.B below, we note that a total of 48 proxy access proposals have received majority votes as of June 20, 2015.

[9] Exchange Act Release No. 8206, 1967 WL 88215 (Dec. 14, 1967).

[10] *See, e.g.*, *Pitney Bowes, Inc.* (avail. Jan. 22, 2013)* (allowing exclusion under Rule 14a-8(i)(9) of a shareholder proposal requesting that the board adopt a policy prohibiting accelerated vesting of equity awards upon a change in control, which conflicted with a company stock plan proposal allowing for accelerated vesting of awards for executives terminated due to a change in control); *Goodrich Corp.* (avail. Jan. 27, 2004) (allowing exclusion under Rule 14a-8(i)(9) of a proposal requesting that the company utilize performance- and time-based restricted share programs in lieu of stock options for future senior executive equity compensation, which conflicted with a proposal to amend the company's stock option plan by increasing the securities available for issuance under the plan); *INTERLINQ Software Co.* (avail. Apr. 20, 1999) (allowing exclusion under Rule 14a-8(i)(9) of a proposal for the

company to conduct a self-tender offer, which conflicted with a merger proposal to be included in the same proxy materials).

[11] Letter from the Ann Yerger, Executive Director, Council of Institutional Investors, to Keith F. Higgins, Director, Division of Corporation Finance, SEC (Jan. 9, 2015), *available here*.

[12] Statement from Chair White Directing Staff to Review Commission Rule for Excluding Conflicting Proxy Proposals (Jan. 16, 2015), *available at* http://www.sec.gov/news/statement/statement-on-conflicting-proxy-proposals.html; Announcement of the Division of Corporation Finance Related to Exchange Act Rule 14a-8(i)(9) for Current Proxy Season (Jan. 16, 2015)**,** *available at* http://www.sec.gov/corpfin/announcement/cf-announcement---rule-14a-8i9-no-views.html.

[13] On February 13, 2015, Whole Foods announced that it had postponed its 2015 Annual Meeting of Stockholders in response to the Staff's review of Rule 14a-8(i)(9). On June 26, 2015, Whole Foods announced that its bylaws had been amended to adopt proxy access with a 3%/3-year threshold. The shareholder proponent subsequently withdrew his proposal.

[14] Mary Jo White, Chair, SEC, Address at the Tulane University Law School 27th Annual Corporate Law Institute (transcript available at http://www.sec.gov/news/speech/observations-on-shareholders-2015.html).

[15] Other proponents, including union pension funds, supported the Comptroller's initiative by submitting proxy access shareholder proposals this season as well. Most of these proposals are identical or very similar to the Comptroller's proposals. In addition, individual shareholders who in prior years had submitted proxy access shareholder proposals urging a 1%/1-year eligibility standard, submitted proposals for the 2015 proxy season urging adoption of proxy access bylaws with a 3%/3-year eligibility standard.

[16] One of these companies, Nabors Industries Ltd., had previously adopted a proxy access corporate governance policy that was not included in the company's bylaws.

[17] This category includes the proxy access shareholder proposal that was excluded after the Staff concurred that the company had substantially implemented the proposal. *See General Electric Co. (Recon.)* (avail. Mar. 3, 2015)* (concurring in the exclusion under Rule 14a-8(i)(10) of a proxy access proposal after the board adopted a proxy access bylaw consistent with the "essential objective" of the shareholder proposal).

[18] Arch Coal, Cabot Oil & Gas, Marathon Oil, HCP, CF Industries Holdings, Boston Properties, New York Community Bancorp, and Priceline Group.

[19] AES, Exelon, Chipotle, Cloud Peak Energy, Expeditors International of Washington, SBA Communications, and Visteon.

[20] Outside of the proxy access context, at one company where both a company-sponsored proposal and a shareholder proposal to provide shareholders the ability to call special meetings received more than a majority of the votes cast. The company-sponsored proposal was supported by 76% of the company's outstanding shares, which was below the 80% approval required for the proposal to amend the company's certificate of incorporation. In contrast, the shareholder proposal was supported by 52% of the votes cast, which represented only 43% of the company's outstanding shares.

[21] *Express Scripts Holding Co. v. Chevedden*, 2014 U.S. Dist. LEXIS 19689 (E.D. Mo. Feb. 18, 2014).

[22] *See, e.g.*, *Verizon Communications Inc. (Kenneth Steiner)* (avail. Jan. 15, 2014) (denying exclusion where company argued that the supporting statement contained several false statements about the company's corporate governance and executive compensation); *Starbucks Corp.* (avail. Dec. 23, 2013)* (denying exclusion where company argued that the supporting statement included multiple false statements about the company's corporate governance and labor practices).

[23] *Ferro Corp.* (avail. Mar. 17, 2015).

[24] *Id.*

[25] *See AT&T, Inc.* (avail. Dec. 11, 2014, *recon. denied* Feb. 10, 2015). The proposal sought a 10% minimum threshold for special shareholder meetings and contained three alleged false statements justifying the proposal. One of the proposal's statements, highlighting a "complete absence of provisions for shareholders to act by written consent," contradicted the company's articles of incorporation and yet the Staff did not concur with exclusion on Rule 14a-8(i)(3) grounds.

[26] In response to Pfizer's no action request, Mr. Chevedden submitted a supplemental letter arguing that the independence standard in the proposal submitted to Pfizer was substantively identical to the standard in the independent chair proposal in *Mylan Inc.* (avail. Jan. 16, 2014) in which Mylan had argued that certain terminology, including the words "nontrivial," and "professional," were vague and indefinite. The Staff had refused to concur with the exclusion of the *Mylan* proposal.

[27] *See*, *e.g.*, *Abbott Laboratories* (avail. Feb. 26, 2015); *The Boeing Co.* (avail. Feb. 26, 2015, *recon. denied* Mar. 4, 2015). The Staff did not change its concurrence in *Pfizer* because by the time the proponents asked for reconsideration, Pfizer already had started printing its proxy materials; thus the Staff determined that reconsideration would result in "significant cost and could threaten the timing of its delivery of proxy materials." *Pfizer Inc*. (avail. Feb. 18, 2014, *recon. denied* Mar. 10, 2014).

[28] *Bank of America Corp.* (avail. Mar. 6, 2014)*.

[29] *See* Hannah Ishmael, *Gilead Sciences, Inc. and Vertex Pharmaceuticals Incorporated: UAW Trust Pricing Proposal Now Put to Shareholder Vote*, Bidness Etc (Mar. 14, 2015, 8:55am), *available at* http://www.bidnessetc.com/36910-gilead-sciences-inc-and-vertex-pharmaceuticals-incorporated-uaw-trust-prici/.

[30] *See Gilead Sciences, Inc.* (avail. Feb. 23, 2015); *Vertex Pharmaceuticals, Inc.* (Feb. 25, 2015); *Celgene Corp.* (avail. Mar. 19, 2015).

[31] *Bristol-Myers Squibb Co.* (avail. Feb. 21, 2000) and *Eli Lilly and Co.* (avail. Feb. 25, 1993).

[32] *See Costco Wholesale Corp.* (avail. Nov. 14, 2014, *recon. denied* Jan. 5, 2015); *Deere & Co.* (avail. Nov. 14, 2014, *recon. denied* Jan. 5, 2015); *The Walt Disney Co.* (avail. Nov. 24, 2014, *recon. denied* Jan. 5, 2015).

[33] *See, e.g.*, *Pfizer Inc.* (avail. Dec. 19, 2014); *The Home Depot Inc.* (avail. Jan. 30, 2014)*.

[34] *See Bristol-Myers Squibb Company* (avail. Jan. 7, 2015); *Lowe's Companies, Inc.* (avail. Mar. 10, 2015); *YUM! Brands, Inc.* (avail. Jan. 7, 2015, *recon. denied* Feb. 26, 2015); *Wal-Mart Stores, Inc.* (avail. Mar. 16, 2015).

[35] *See Trinity Wall Street v. Wal-Mart Stores, Inc.*, No. 14-4764, 2015 WL 1905766 (3d Cir. Apr. 14, 2015). Gibson Dunn represented Wal-Mart at trial before the district court and on appeal before the Third Circuit.

[36] No. 14-405-LPS, 2014 WL 6790928, at *1-2 (D. Del. Nov. 26, 2014).

[37] *See Trinity Wall Street v. Wal-Mart Stores, Inc.,* No. 14-4764 (3d Cir. July 6, 2015). The Third Circuit's opinion was released one week before the July 13 deadline for Trinity to seek leave to appeal the Third Circuit's judgment to the U.S. Supreme Court. On July 10, Trinity moved for, and was granted, an extension of its time to file a petition for a writ of certiorari. Trinity now has until September 11, 2015 to file a petition seeking leave to appeal to the U.S. Supreme Court.

[38] *Id* at *2. The products cited by the proposal included any products that endanger "public safety and well-being," that have "the substantial potential to impair the reputation of the [c]ompany," or that could be considered "offensive" to "family and community values."

[39] *Id* (internal quotation marks omitted).

[40] *Id*.

[41] *Id* at *8-9.

[42] Appellant's Opening Brief, No. 14-4764, at 6 (3d Cir. Jan. 14, 2015). Wal-Mart also filed a supplemental letter highlighting the Staff's decision in *Rite Aid Corp.* (avail. Mar. 24, 2015). In *Rite Aid*, the Staff concurred with exclusion on the basis of Rule 14a-8(i)(7) of a proposal that was identically worded in all material respects. Wal-Mart indicated that the Staff's decision in *Rite Aid* further underscored that the District Court erred in holding that Trinity's proposal was not excludable under Rule 14a-8(i)(7).

Gibson, Dunn & Crutcher's lawyers are available to assist in addressing any questions you may have about these developments. To learn more about these issues, please contact the Gibson Dunn lawyer with whom you usually work, or any of the following lawyers in the firm's Securities Regulation and Corporate Governance practice group:

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