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The 1983 Amendments to SEC Rule 14A-8: Upsetting a Precarious Balance

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THE 1983 AMENDMENTS TO SEC RULE 14a-8: UPSETTING A PRECARIOUS BALANCE

I. INTRODUCTION

The central purpose of the federal securities laws, which apply to publicly-held corporations, is disclosure.¹ The rationale for disclosure is to provide shareholders with sufficient information to make intelligent decisions and to apprise them of significant developments within the company.² Consistent with this goal, the shareholder proposal rule³ aids the shareholder as a voter by enlarging the scope of information he receives, by permitting him to propose policy questions for the benefit of fellow shareholders, and by allowing him to vote on questions proposed by other shareholders.⁴

Due to the size and dispersion of the shareholder body in large publicly-held companies, a surrogate mechanism is necessary to allow shareholders to be represented at the annual shareholders' meeting.⁵ It is simply not practical for all or even a majority of the shareholders to be present at the annual meeting to vote on matters of corporate concern.⁶ Allowing shareholders to vote by proxy alleviates this problem. A proxy is nothing more than an agency relationship created when a shareholder authorizes the holder of his proxy to cast his vote

1. Cohen, *The SEC and Proxy Contests*, 20 FED. B. J. 91, 94 (1960); Loomis, *The Securities Exchange Act of 1934 and the Investment Advisors Act of 1940*, 28 GEO. WASH. L. REV. 214 (1959).

2. Von Mehren & McCarroll, *The Proxy Rules: A Case Study in Administrative Process*, 29 LAW & CONTEMP. PROB. 728, 730 (1964).

3. 17 C.F.R. § 240.14a-8 (1984). Reprinted in appendix. The shareholder proposal rule, commonly referred to as the "shareholder bill of rights," requires management to include in its proxy statement a proposal submitted by a stockholder if the proposal is a proper subject for action by the shareholder. E. ARANOW & H. EINHORN, *PROXY CONTESTS FOR CORPORATE CONTROL* 281 (2d Ed. 1968). By means of this rule, the shareholder has the opportunity, at almost no cost to himself, to reach the great majority of shareholders in larger public corporations who choose to vote by proxy rather than attend the stockholders meetings. Note, *Proxy Rule 14a-8: Omission of Shareholder Proposals*, 84 HARV. L. REV. 700 (1971).

4. Latham & Emerson, *Proxy Contest Expenses and Shareholder Democracy*, 4 CASE W. RES. 5, 9 (1952).

5. Schwartz & Weiss, *An Assessment of the SEC Shareholder Proposal Rule*, 65 GEO. L.J. 635 (1977).

6. L. SOLOMON, R. STEVENSON, D. SCHWARTZ, *CORPORATIONS* 461 (1982) [hereinafter cited as SOLOMON].

at the annual meeting.⁷ The proxy rules promulgated by the Securities Exchange Commission⁸ (Commission) under section 14 of the Securities Exchange Act of 1934⁹ are primarily concerned with how this agency relationship is created and what facts the shareholder must be given by those seeking his proxy so that he may have sufficient information for an intelligent vote.¹⁰ Indeed, the major premise of the shareholder proposal rule is that, to achieve true corporate democracy, the issuer's materials should be as much a forum for proper shareholder proposals as it is for management's proposals.¹¹ Under Rule 14a-8 a shareholder can, subject to certain limitations, submit a proposal for inclusion in the corporate proxy material which will later be voted on by fellow shareholders.

Congress created the Commission, in part, to prevent the recurrence of abuses which frustrated the shareholders' free exercise of voting rights and to insure "fair corporate suffrage."¹² The Commission's Proxy Review Program strives to further this goal.¹³ Consistent with this broad goal, the Proxy Review Program seeks to reduce disclosure costs, streamline the proxy rules, and improve proxy readability.¹⁴ However, accomplishing these objectives while insuring

7. Von Mehren & McCarrol, *supra* note 2, at 729. Under the common law, shareholders were largely prohibited from voting by proxy unless permitted in the corporation's articles or by-laws. However, today all corporate statutes permit shareholders to vote by proxy, even in the absence of an article or by-law amendment. *See generally*, M. EISENBERG, *THE STRUCTURE OF THE CORPORATION - A LEGAL ANALYSIS* 99 (1976).

8. The Securities and Exchange Commission has the responsibility of administering and enforcing the federal securities laws. It is an independent regulatory agency consisting of five members appointed for staggered five year terms by the President with the concurrence of the Senate. H. BLOOMENTHAL, *1984 SECURITIES LAW HANDBOOK* 1 (1984).

9. 15 U.S.C. § 78a-78 KK (1976).

10. Von Mehren & McCarrol, *supra* note 2, at 729.

11. Heller, *Stockholder Proposals*, 4 VA. L. WEEKLY DICTA COMPILATION 70 (1953).

12. H.R. Rep. No. 1383, 73d Cong., 2d Sess. 13-14 (1934).

Fair corporate suffrage is an important right that should attach to every equity security bought on a public exchange. Management of properties owned by the investing public should not be permitted to perpetuate themselves by the misuse of corporate proxies. Insiders having little or no substantial interest in the properties they manage have often retained their control without an adequate disclosure of their interests and without an adequate explanation of the management policies they intended to pursue.

Id. *See* Securities Exchange Act 1934, § 14(a), 15 U.S.C. § 78 n(a) (1976).

13. The Commission's Proxy Review Program is designed to reduce the burdens of compliance with the Commission's proxy rules consistent with investor protection. Securities Exchange Act of 1934 Release No. 34-19135 (Oct. 12, 1982), 47 Fed. Reg. 27420 (1982), 26 SEC DOCKET (CCH) 494 (1982). [hereinafter cited as SEC DOCKET].

14. *Id.* at 496. *See also* Karmel, *Proxy Review Program Designed to Ease Burdens*, SEC '83 9 (1982).

that Rule 14a-8 continues to serve fairly both the issuers and the shareholders is no easy task.

The Commission must seek an appropriate balance between providing shareholders with reasonable access to the issuer's proxy machinery and protecting issuers from abuses resulting from shareholder access.¹⁵ Not surprisingly, issuers have generally advocated limiting shareholder access to corporate proxy materials.¹⁶ In contrast, shareholders frequently contend that the shareholder proposal rule is the only device they can employ to influence corporate decisions.¹⁷ Many shareholders believe that Rule 14a-8 improves the relationship between management and shareholders.¹⁸

Issuers and some commentators frequently express their concern that the shareholder proposal rule serves no useful purpose.¹⁹ A common misconception held by them is that shareholder proposals are merely safety valves through which irate shareholders express their concerns.²⁰ In reality, however, many shareholders use proposals as a device for funnelling new information and injecting new perspectives into the corporation, often subtly affecting company decisions.²¹ Today, the shareholder is more literate and perceptive than even the most visionary proponent of the original shareholder proposal rule could have predicted.²² Therefore, management's traditional argument

15. Schwartz & Weiss, *supra* note 5, at 638.

16. Lydenberg, *High Noon for Social Proxy Activists*, 46 BUS. SOC'Y. REV. 62 (1983).

17. Schwartz & Weiss, *supra* note 5, at 635. Absent the shareholder proposal rule all corporate media are solely in the hands of management. Thus, "[w]ithout the benefit of this rule, a shareholder who is dissatisfied with his company's behavior and is without sufficient funds to solicit proxies, will find effective communication with his fellow shareholders impossible." Schulman, *Shareholder Cause Proposals: A Technique to Catch the Conscience of the Corporation*, 40 GEO. WASH. L. REV. 41 (1971).

18. Propp, *The SEC's Shareholder Proposal Rule: Corporate Accountability at the Crossroads*, 11 SEC. REG. L.J. 99, 133 (1983).

19. Division of Corporation Finance, *Summary of Comments: Shareholder Proposal Release 15* (1983) (available in Valparaiso University Law School Library) [hereinafter cited as *Summary of Comments*].

20. Propp, *supra* note 18, at 128.

21. *Id.* at 99. Under Rule 14a-8, the Commission, through the staff of the Division of Corporation Finance, functions as an intermediary between proponents and issuers. Expedient scrutiny of proposals is facilitated by referral of the material to the staff members. Consequently, "[t]he role of the Commission approaches more nearly that of an umpire fixing the rules, detecting the infraction, and applying the remedy whether it be correction by retraction or explanation or by process of the court." Cohen, *supra* note 1, at 102.

22. Latham & Emerson, *supra* note 4, at 8. In fact, "much evidence is at hand that the stockholder along with his fellow members of the general public are being educated and experiencing an awakening of the breadth of his intellectual capacities for corporate as well as general understanding." *Id.*

that shareholder input need only be sought for fundamental economic decisions is no longer valid. Unfortunately, some issuers feel that this increasingly sophisticated class of investors is currently abusing the shareholder proposal system.²³

In an apparent attempt to respond to criticism that shareholder proponents are currently abusing the shareholder proposal process, the Commission recently revised Rule 14a-8.²⁴ The revisions adopted by the Commission are significant and evidence an intent to tighten up the provisions of the shareholder proposal rule.²⁵ In particular, the recent amendments attempt to eliminate the alleged abuse by "sophisticated investors" by placing arbitrary barriers before shareholders seeking access to the corporate proxy machinery.²⁶ This practice of arbitrarily restricting shareholder access to the proxy machinery, coupled with management's relatively unfettered access to that machinery, only perpetuates the legal separation of ownership from control.²⁷ In the words of a current commissioner, "[i]f we are going to support shareholder access in theory, we should support it in practice as well, and not just for highly sophisticated investors who can afford to develop or retain the skills necessary to master the labyrinth that Rule 14a-8 sets before them."²⁸ Hence, if the shareholder proposal process is to work effectively, the Commission must be careful to assure that it is operated in a balanced, neutral manner.

This note examines the current revisions adopted by the Commission to Rule 14a-8 as well as the legislative policy that the shareholder proposal rule was initially designed to embody. This legislative policy is examined in light of the legislative history and early Commission interpretation of case law. This note then explores the reasons why the present revisions, taken collectively, fail adequately to serve that policy. Finally, this note suggests some revisions, workable within the previous framework of Rule 14a-8, which will comport with both the goals of the Proxy Review Program and the original legislative policy.

23. See generally, *Summary of Comments*, *supra* note 19.

24. Securities Exchange Act of 1934 Release No. 34-20091 (Oct. 13, 1983), 47 Fed. Reg. 47,420 (1983) (Longstreth, Comm., Dissenting) [hereinafter cited as Release No. 34-20091].

25. Lydenberg, *supra* note 16, at 64.

26. Release No. 34-20091, *supra* note 24, at 8. See *infra* notes 263-448 and accompanying text.

27. Elliot, *The Remarriage of Corporate Ownership and Management Accountability*, 3 U. BRIDGEPORT L. REV. 49 (1981).

28. Release No. 34-20091, *supra* note 24, at 8.

II. HISTORICAL PERSPECTIVE AND UNDERLYING RATIONALES OF RULE 14a-8

Rule 14a-8,²⁹ the shareholder proposal rule, is one of the most widely known rules administered by a federal agency.³⁰ The rule permits any shareholder who complies with its provisions, and whose purpose does not fall within the categories which may be omitted from an issuer's proxy material, to propose action to be voted on by his fellow shareholders.³¹ However, "[t]he right of a shareholder to have his proposal included in the issuer's proxy material is less than absolute."³² The question of whether a proposal is a proper subject for inclusion in the proxy statement has plagued the Commission for many years.³³ To fully appreciate the significance of the present revisions to Rule 14a-8 one must examine the evolution of the shareholder proposal rule.

Section 14(a)³⁴ of the 1934 Securities Exchange Act³⁵ empowers the Commission to regulate the solicitation of proxies³⁶ from holders

29. 17 C.F.R. § 240.14a-8 (1984) *Reprinted in* appendix.

30. Black & Sparks, *The SEC as Referee — Shareholder Proposals and Rule 14a-8*, 2 J. CORP. LAW 1 (1976).

31. *Id.* at 2.

32. Comment, *SEC Shareholder Proposal Rule 14a-8: Impact of the 1972 Amendments*, 61 GEO. L.J. 781, 782 (1973). Under state law, shareholders have never been granted the right to have a proposal included in the corporate proxy materials even though the proposal might properly be considered at the annual meeting. The Commission affords shareholders an opportunity, not available at state law, for participation in corporate affairs. Note, *Proxy Rule 14a-8: Omission of Shareholder Proposals*, 84 HARV. L. REV. 700, 703 (1971).

33. Schwartz, *The Public Interest Proxy Contest: Reflections on Campaign GM*, 69 MICH. L. REV. 421, 436 (1971).

34. Securities Exchange Act of 1934, § 14(a), 15 U.S.C. § 78 n(a) (1976). [I]t shall be unlawful for any person, by use of mails or by any means or instrumentality of interstate commerce or of any facility of a national securities exchange or otherwise, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security other than an exempted security.

Id.

35. Securities Exchange Act of 1934, 15 U.S.C. § 78a-78KK (1976). Congress authorized the creation of the Commission to prevent the recurrence of abuses which have frustrated the free exercise of the voting rights of stockholders. H.R. Rep. No. 1383, 73d Cong., 2d Sess. 14 (1934).

36. The term "proxy" includes every proxy, consent or authorization within the meaning of section 14(a) of the Securities Exchange Act of 1934. The consent or authorization may, however, take the form of failure to object or dissent. R. HAMILTON, *CORPORATIONS* 528 (2d Ed. 1981).

of securities registered on national securities exchanges.³⁷ Congress provided the Commission with broad authority³⁸ to adopt rules regulating the solicitation of proxies in order to promote "fair corporate suffrage."³⁹ In 1935, the Commission adopted its first set of rules known as the "L.A. Rules."⁴⁰ After three proxy seasons⁴¹ the Commission formulated a comprehensive set of rules denominated Regulation X-14.⁴² This regulation included a general anti-fraud provision which stated that if management was aware of any action proposed to be taken at the annual corporate meeting pertaining to any

37. Heller, *supra* note 11, at 72. Section 14 is applicable to all securities registered in accordance with § 12, 15 U.S.C. § 78 L (1976). Under § 12(g) (1-2), all companies whose stock is traded on a national exchange, or that have assets in excess of \$3 million and more than 300 shareholders of record, are subject to the periodic reporting and proxy regulations of § 14. 17 C.F.R. § 240.12g 1-2 (1984). However, the Commission has expressly removed certain solicitations from the ambit of proxy regulations. 17 C.F.R. § 240.14a-2 (1984).

38. Section 14(a) authorizes the Commission to adopt rules "... as necessary or appropriate in the public interest and for the protection of investors...." 15 U.S.C. § 78 N (a) (1976). "Thus in effect Congress left the entire problem of the nature, extent and form of the federal proxy regulation for the SEC to consider and solve, and the proxy rules as they have evolved since 1934, represent the SEC's exercise of delegated power." Von Mehren & McCarrol, *supra* note 2, at 729.

39. See *supra* note 12.

In order that the stockholder may have adequate knowledge as to the manner in which his interests are being served, it is essential that he be enlightened not only as to the financial condition of the corporation, but also to the major questions of policy, which are decided at stockholder meetings. Too often proxies are solicited without explanation to the stockholder of the real nature of the questions for which authority to cast his vote is sought.

S. Rep. No. 1455, 73d Cong., 2d Sess. 77 (1934).

40. Securities Exchange Act of 1934 Release No. 378 (Class A) (July 8, 1942), 7 Fed. Reg. 5209 (1942). The "L.A. Rules" required the issuance of a proxy statement containing a "brief description" of the matters to be considered at the stockholders' meeting. Further, it prohibited false or misleading statements, required the filing of proxy materials at the time they were mailed to the stockholders, and required management to mail out proxy materials submitted by stockholders. E. ARANOW & H. EINHORN, *supra* note 3, at 92. Essentially, the rules were nothing more than a set of principles which permitted the Commission to control the most blatant abuses while studying further the needs and requirements of the problems which Congress had given to them. Von Mehren & McCarrol, *supra* note 2, at 736.

41. The proxy season is the first three or four months of the new year, when companies operating on a calendar basis hold their annual meeting. During this time, the Commission receives a good portion of correspondence dealing with shareholder proposals. Dean, *Non-Compliance With Proxy Regulations: Effect on Ability of a Corporation to Hold Valid Meeting*, 24 CORNELL L.Q. 483, 493 (1939).

42. Securities Exchange Act of 1934 Release No. 1823 (Aug. 11, 1938), 3 Fed. Reg. 1991 (1938). See generally, Note, *Shareholder Proposals: The Experience of Rule 14a-8*, 59 GEO. L.J. 1343, 1344-45 (1971).

matter not otherwise disclosed, it would be obligated to describe briefly the substance of each matter in its communications to shareholders.⁴³ However, the Commission had yet to promulgate a specific shareholder proposal rule.

In 1942, the Commission promulgated the first rule regulating shareholder proposals.⁴⁴ The rule, known as X-14a-7, required management to include in the proxy statement any shareholder proposal which was a "proper subject" for action by security holders.⁴⁵ In the Commission's view, the term "proper subject" would be interpreted according to the laws of the issuer's domicile.⁴⁶ The "state law standard" required the Commission to study the statutory and decisional

43. This provision stated:

No solicitation subject to Section 14(a) of the act shall be made by means of any form of proxy, notice of meeting, or other communication containing any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact necessary in order to make the statements therein not false or misleading.

Rule X-14 a-5, Release No. 1823, *supra* note 42. The Commission first stated in 1939, and continues to believe, that a proxy statement which fails to disclose all matters which management believes will properly be put before shareholders as well as how management intends to vote the proxies which it solicits, is misleading. *Hearing on SEC Proxy Rules Before the House Committee on Interstate and Foreign Commerce*, 78th Cong., 1st Sess. 169-70 (1943).

44. Securities Exchange Act of 1934 Release No. 3347 (Dec. 18, 1942), 7 Fed. Reg. 10,653 (1942). At the hearings before the House Interstate and Foreign Commerce Committee, Chairman Purcell explained an underlying reality that prompted adoption of the rule:

Once a shareholder could address a meeting, today he can only address the assembled proxies which are lying at the head of the table. The only opportunity that the stockholder has of expressing his judgment comes at the time when he considers the execution of the proxy form, and we believe, whether we are right and whether we are wrong — and I think we are right — that that is the time he should have the full information before him and the ability to take action as he sees fit.

The proxy solicitation is now in fact the only means by which a stockholder can act and can perform the functions which are his as owner of the corporation. It, therefore, seems clear to us that only by making the proxy a real instrument for the exercise of those functions can we obtain what the Congress and this committee called for in the form of "fair corporate suffrage."

Hearings on H.R. 1493, H.R. 1821, and H.R. 2019, Before the House Committee on Interstate and Foreign Commerce, 78th Cong., 1st Sess., pt. 2, at 174-75 (1943).

45. *Id.*

46. Securities Exchange Act Release No. 3638 (Jan. 3, 1945), 11 Fed. Reg. 10,995 (1946). The Director of the Division of Corporate Finance issued an opinion stating: Speaking generally, it is the purpose of rule X-14 a-7 to place stockholders

law of the state of incorporation and discover each state's interpretation.⁴⁷ However, the lack of case law on shareholder authority forced the Commission to rely heavily on state corporation statutes.⁴⁸ Unfortunately, most state corporation statutes contained only broad and cryptic language with respect to the duties of the board of directors.⁴⁹ The consequence of relying on state law to determine the scope of the federal remedy created many problems and was soon challenged.⁵⁰

The first important corporate challenge to the Commission's power over the proxy solicitation process occurred in 1947.⁵¹ In *SEC*

in the position to bring before their fellow stockholders matters of concern to them as stockholders in such corporation; that is, such matters relating to the affairs of the company concerned as are proper subjects of stockholders' action under the laws of the state under which it was organized. It was not the intent of rule X-14 a-7 to permit stockholders to obtain the consensus of other stockholders with respect to matters which are of a general political, social or economic nature. In short, rule X-14 a-7 should operate so as to leave intact the primary substantive regulation which state law seeks to achieve.

Id.

47. *Id.* Schwartz & Weiss, *supra* note 5, at 654.

48. The purpose of the relevant state statutory provisions was merely to empower proxy voting, not to regulate its mechanics. While the proxy system grew in significance and complexity, the corporation statutes failed to adequately regulate the solicitation of proxies. Indeed, the presence of the proxy rules issued by the Commission and its central administrative mechanism for enforcing them may account in part for the inaction of state legislatures in this area. Eisenberg, *Access to Corporate Proxy Machinery*, 83 HARV. L. REV. 1492-93 (1970).

49. Section 141(a) of the Delaware General Corporation Law states: "[t]he business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation" DEL. CODE ANN. tit. 8 § 141(a) (Supp. 1980). The principal draftsman of the Delaware Incorporation Statute, Professor Ernest L. Folk, has observed that in Delaware the corporation "enjoys the broadest grant of power in the English-speaking world to establish the most appropriate internal organization and structure for the enterprise." E. FOLK, AMENDMENTS TO THE DELAWARE GENERAL CORPORATION LAW 5 (1969).

50. Interpretation of state law would seem to place the SEC in much the same position as the federal courts in the latter's application of the *Erie* Doctrine. Because there are few decisions on shareholders' authority under state law, the only guidelines available are the corporation statutes which normally contain very broad language with respect to the roles of directors and shareholders. The North Carolina statute, though broad, is considerably more explicit than most: "Any matter relating to the affairs of a corporation is a proper subject for action at an annual meeting of shareholders."

N.C. GEN. STAT. § 55-61 (d) (1982). See also DEL. CODE ANN. tit. 8 § 141(a) (Supp. 1980). See Note, *supra* note 42, at 1347.

51. Note, *Permissible Scope of Stockholder Proposals Under SEC Proxy Rules*, 57 YALE L.J. 874 (1948).

v. Transamerica, a conflict arose between a corporate by-law and the Commission's shareholder proposal rule.⁵² The corporate by-law gave management virtually unlimited power to omit shareholder proposals submitted in the form of a by-law amendment unless proper notice was given.⁵³ The Court of Appeals for the Third Circuit affirmed that a "proper subject" should be determined by reference to state corporation statutes instead of corporate by-laws.⁵⁴ The court endorsed the notion that the power conferred upon the Commission by Congress cannot be frustrated by procedural devices valid under state law for other purposes.⁵⁵ However, applicable state corporation law, recognized as the appropriate guide for shareholder resolutions, offered little guidance.

The Commission then developed a federal common law as a substitute for state law guidance.⁵⁶ The Commission assumed an interpretive role in the absence of state law;⁵⁷ although the Commission was mindful of the necessity to avoid stripping the board of directors of its basic governing function.⁵⁸ The shareholder proposal rule, though, still did not specify any particular circumstances under which management could properly omit a shareholder proposal.

Following the *Transamerica* decision, the Commission began to define and limit the parameters of what is a proper subject under the shareholder proposal rule.⁵⁹ The Commission perceived that some

52. 163 F.2d 511 (3d Cir. 1947), *cert. denied*, 332 U.S. 847 (1948). A shareholder informed management of his intention to submit four proposals for inclusion in the corporate proxy material. Management attempted to exclude the proposals claiming that the shareholder failed to comply with notice provisions in the company by-laws. The Commission sued to enjoin the proxy solicitation, arguing that Transamerica was not entitled to use its notice by-law "as a block or strainer to prevent any proposal to amend the by-laws, which it may deem unsuitable, from reaching a vote at the annual meeting of stockholders." *Id.* at 515. The court held that the proposals were proper subjects under Delaware's general corporation laws. *Id.* at 518.

53. *Id.* at 514.

54. *Id.* at 517.

55. *Id.* at 518. The court then added that it would not permit a notice by-law to eviscerate the SEC's proxy rules:

If this minor provision may be employed as Transamerica seeks to employ it, it will serve to circumvent the intent of Congress in enacting the Securities Exchange Act of 1934. It was the intent of Congress to require fair opportunity for the operation of corporate suffrage. This control of great corporations by a very few persons was the abuse at which Congress struck in enacting Section 14(a).

Id.

56. Schwartz, *supra* note 33, at 440.

57. Propp, *supra* note 18, at 104.

58. Schwartz, *supra* note 33, at 440.

59. In adopting the 1948 release, the Commission indicated for the first time that

shareholder proponents were abusing the shareholder proposal process.⁶⁰ In 1948, the Commission amended the shareholder proposal rule.⁶¹ The amendment allowed an issuer to omit proposals submitted "primarily for the purpose of enforcing a personal claim or redressing a personal grievance."⁶² This attitude was the Commission's underlying rationale in a no-action letter issued by the staff in 1951.⁶³

In *Greyhound v. Peck*⁶⁴ a federal district court upheld the staff's no-action determination.⁶⁵ The court, relying on a previous Commission release,⁶⁶ concurred with both the staff and management that a

under certain circumstances a proposal relating to a matter which was a "proper subject" under state law could nevertheless be omitted from the proxy statement. Schwartz & Weiss, *supra* note 5, at 655.

60. Ledes, *A Review of Proper Subject Under the Proxy Rules*, 34 U. DET. L. REV. 520, 522 (1957). The Commission changed the rule in order to prevent abuses of Rule 14a-8 by persons seeking personal ends to the detriment of the security holders. *Id.*

61. Securities Exchange Act of 1934 Release No. 4185 (July 6, 1948), 13 Fed. Reg. 3973 (1948).

62. The Commission's release announcing the adoption of the amendment explained:

This rule requires management to include in its proxy material, proposals reasonably submitted by security holders which are proper subjects for action by security holders. The Commission has found that in a few cases security holders have abused this privilege by using the rule to achieve personal ends which are not necessarily in the common interests of the issuer's security holders generally.

Id. Additional criteria under which management could properly omit proposals were included in the amendment. They were:

1.) If management had included a shareholder's proposal in its proxy statement in the previous two years and the shareholder without good cause failed to attend the annual meeting to present the proposal; 2.) if substantially the same proposal had been presented at the last annual or special meeting and had failed to receive 3% of the total number of votes cast.

Id. Finally, this amendment required management, in order to omit a proposal, to submit its reasons to the Commission and notify the shareholder at the same time. Ledes, *supra* note 60, at 522.

63. Letter to Greyhound, dated March 8, 1951. In a no-action letter, the staff essentially states that it will not recommend that the Commission take action if the shareholder proposal is omitted from the corporate proxy material. The staff will ordinarily advise both the issuer and the proponent of the staff's view concerning management's position with respect to a proposal. However, there is no requirement that the issuer or the proponent adhere to the conclusion expressed by the staff. In addition, no-action letters lack any precedential value.

64. 97 F. Supp. 679 (S.D.N.Y. 1951). The shareholder proponent, owner of three shares of stock, requested that there be included in Greyhound's proxy material the following proposal: "[a] recommendation that management consider the advisability of abolishing the segregated seating system in the south." *Id.* at 680.

65. *Id.*

66. Securities Exchange Act Release No. 4775 (Dec. 11, 1952), 17 Fed. Reg. 11,431 (1952). The amendment also required that stockholder proposals be submitted thirty days

shareholder proposal of a general, political, social, or economic nature was properly excludable from Greyhound's corporate proxy material.⁶⁷ The court held that much deference will be given a staff determination because of the staff's expertise in the securities area.⁶⁸ In *Greyhound*, the court noted that other forums existed for the presentation of such views.⁶⁹ As a result, much impetus existed for codifying such an exclusion.

Primarily as a result of *Greyhound*, the Commission in 1952 revised the shareholder proposal rule.⁷⁰ Issuers could now omit proposals submitted, "primarily for the purpose of promoting general

before the time of the previous year's proxy solicitation instead of thirty days before the time of the last meeting. In addition, there was a change in the description of the 100 word supporting statement to the effect that the statement need only be in support of the proposal, and not necessarily contain specific reasons in support of the proposal. *Id.*

67. 97 F.Supp. at 680.

68. Rules and regulations adopted by the administrative agencies pursuant to Congressional authorization are best interpreted, in the first instance, by the agency which has been entrusted with the power and authority to right them. . . . This court cannot hold, on the proof before it, unaided as it is by the vast experience of daily contact with the practical working of this rule (which the Commission has had) that the interpretation should be set aside

Id. at 681. This statement implies that the administrative rather than the legal expertise should be the controlling factor in the construction and interpretation of the shareholder proposal rule. Note, *supra* note 42, at 1343. The considerable respect paid to a Commission determination may be the logical result of the manner in which the issues are brought before the court when a plaintiff shareholder seeks to enjoin company action. The court, presented only with the argumentative briefs prepared by opposing counsel, and with no possibility of remanding the case to the agency, may be justifiably reluctant to disturb the Commission's ruling. *Id.* In *Dyer v. SEC*, 287 F.2d 773, 779 (8th Cir. 1961), the court pointed out that:

The Commission's judgment as to necessity or appropriateness is . . . not subject to being judicially scrutinized as a matter of doubt or mere disagreement as to the wisdom of the Commission's actions, but only as a matter of utter lack of any possible rational basis, or of legal arbitrariness, capriciousness, or other administrative irresponsibility having been controlling thereof.

69. The court in *Greyhound* stated that, "[i]t was not the intent of Rule X-14 a-7 (Now Rule X-14 a-8) to permit stockholders to obtain the consensus of other stockholders with respect to matters which are of a general political, social, or economic nature. Other forums exist for the presentation of such views." 97 F. Supp. at 680.

70. Release No. 4775, *supra* note 66. Procedurally, the shareholder proposal rule now provided for: a conclusive presumption of timeliness for any proposal submitted sixty days prior to the release of the proxy material for the last annual meeting; a twenty day notice requirement to shareholders and to the Commission if management intended to omit a proposal; and a 3-6-10 percent resubmission progression that would allow proposals that did not obtain the requisite percentage of votes to be omitted after a number of unsuccessful submissions. For an analysis of the practical consequences of these requirements, see generally, E. ARANOW & H. EINHORN, *supra* note 3.

economic, political, racial, religious, social or similar causes."⁷¹ The "for the purpose of" language suggested that an examination was required not only of the substance of the proposal, but also of the shareholder's motive.⁷² One major shortcoming of the 1952 amendments adopted by the Commission was that they offered little help to issuers receiving proposals dealing with issues entirely within the province of management.

In an attempt to provide additional guidance in dealing with shareholder proposals, the Commission again amended Rule 14a-8 in 1954.⁷³ One of the Commission's chief concerns was to relieve management of the necessity of including in its corporate proxy material shareholder proposals relating to matters falling within the province of management.⁷⁴ Also, the Commission sought to alleviate the apparent confusion of many issuers resulting from the holding in *Transamerica*.⁷⁵ The changes adopted allowed issuers to omit

71. Release No. 4775, *supra* note 66.

72. Serious questions are raised as to whether the Commission is capable of determining motivation, let alone the right of a proponent to respond to management's assertions about his motivation. When this is coupled with the staff's limited expertise in this area, an inquiry into motivation appears to be a dubious activity at best. Comment, *supra* note 32, at 781.

73. Securities Exchange Act of 1934 Release No. 4979 (Jan. 6, 1954), 19 Fed. Reg. 246 (1954).

74. *Id.* See also Schwartz, *supra* note 33, at 433. The American Society of Corporate Secretaries had prepared a report titled *History and Operations of Securities & Exchange Commission Rule Governing Proposals by Stockholders* which stated that "the proposal rule was disrupting the organization of American business, wasting the time of its executives, preventing the annual meeting from accomplishing its normal objective, and putting corporations to an intolerable waste of time and money by forcing them to include in their proxy statements the proposals of shareholders." L. GILBERT, *DIVIDENDS AND DEMOCRACY* 104 (1956).

75. The view of the Commission is indicated in the following quote: The present rule [prior to 1954 amendment] provides for submission of proposals which are proper subjects for action by security holders but does not specifically provide that state law is the standard for determining what is a proper subject for such action. In a prior release, the Commission has so stated. (Securities Exchange Act Release No. 3638 January 3, 1945). To clarify this point, the amended rule specifically provides that a security holder's proposal may be omitted from the management's proxy material if it is one which, under the laws of the issuer's domicile, is not a proper subject for action by security holders.

Release No. 4979, *supra* note 73. "The amended rule specifically provides that state law is to be the standard of eligibility of a proposal under the rule. The Commission wishes to make it clear that it considers this standard consistent with the decision of the Court of Appeals in the case of *SEC v. Transamerica Corporation*. . . ." *Id.* The Commission accomplished this result in the 1954 Amendment essentially codifying the administrative policies since 1942, that a proper subject for security holder action under the applicable

shareholder proposals which were related to "ordinary business operations."⁷⁶ Moreover, the exact parameters of the "ordinary business operations" exclusion would now be determined under the laws of the issuer's domicile.⁷⁷ The Commission observed that the phrase "ordinary business operations" refers to the area or scope of activities and not the significance or importance of such activities.⁷⁸ The amendment was especially significant to shareholder proponents because it placed the burden on the issuer to substantiate that a proposal could be omitted under Rule 14a-8.⁷⁹ The 1954 amendments to Rule 14a-8 provided significant guidance and proved highly effective for a number of years.

The second important challenge to the Commission's power over the proxy solicitation process occurred during the 1960's when shareholder activists pressured the Commission to permit the proxy machinery to be used for social reform.⁸⁰ Advocates of social reform who had previously made the corporation a target of their discontent over social conditions tried instead to use the corporation as a vehicle for social reform.⁸¹ In attempting to respond to the many no-action requests,⁸² the staff experienced continuing problems with the "for the purpose of" language common to both the "personal grievance" and "social causes" exclusions.⁸³ The staff decisions ultimately turned on ascertaining the motive of the shareholder proponent for submitting the proposal;⁸⁴ "[i]n spite of strong reasons not to do so — history,

state law is only one consideration as to whether a proposal may be included. Ledes, *supra* note 60, at 524.

76. Release No. 4979, *supra* note 73.

77. *Hearings on a Report from the SEC on its Problems in Enforcing the Securities Laws Before a Subcomm. of the Senate Committee on Banking and Currency*, 85th Cong., 1st Sess., pt. 1 at 118 (1957).

78. Clusserath, *The Amended Stockholder Proposal Rule: A Decade Later*, 40 NOTRE DAME LAW 36 (1964).

79. The rule places the burden on management to show that a particular security holder's proposal is not a proper one for inclusion in management's proxy material. Where management contends that a proposal may be omitted because it is not proper under state law, it will be incumbent upon management to refer to the applicable statute or case law and furnish a supporting opinion of counsel.

Release No. 4979, *supra* note 73.

80. SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS, 96TH CONG., 2D SESS., SECURITIES AND EXCHANGE COMMISSION STAFF REPORT ON CORPORATE ACCOUNTABILITY, B 151 (Comm. Print 1980) [hereinafter cited as STAFF REPORT].

81. Schwartz, *supra* note 33, at 421.

82. STAFF REPORT, *supra* note 80, at 149. See *supra* note 63.

83. STAFF REPORT, *supra* note 80, at 149.

84. *Id.* As a result, "[n]ot only would 'motive' have to be divined without the

policy, and inexperience in related areas — the SEC has tended to interpret the subparagraphs to require an examination of the proponent's motive."⁸⁵ The Commission continued to focus on problems connected with shareholder proposals concerning public policy issues.

In 1970, a group known as "Campaign GM"⁸⁶ attempted to obtain shareholder approval of several social resolutions through the solicitation of proxies.⁸⁷ The staff held that all but two resolutions could be omitted from the corporate proxy materials.⁸⁸ While the two proposals were motivated by social concerns, they were also valid corporate concerns for shareholders.⁸⁹ The other proposals were disallowed on the grounds that they related to "ordinary business."⁹⁰ Although "Campaign GM" generated substantial public interest,⁹¹ both proposals were later voted down.⁹² However, "Campaign GM" demonstrated that socially motivated proposals could be a valid concern for corporate shareholders.

In 1972, the Commission abandoned the distinction between proposals which were motivated principally by concerns of public policy as opposed to corporate policy.⁹³ This shift in attitude was largely the result of *Medical Committee for Human Rights v. SEC*.⁹⁴ The Court

mechanics of a hearing or evidence, but so would whether such motive was the primary one." Schwartz, *supra* note 33, at 446.

85. Schwartz, *supra* note 33, at 448. This policy has resulted in some public-interest questions being excluded from management's proxy statement although they dealt with a subject matter that another shareholder might be allowed to raise. *Id.*

86. The goals of "Campaign GM" were to promote corporate responsibility and to educate management and the public about the social role of corporations. *Id.*

87. Nine resolutions were proposed to management, but the campaign was largely an effort to obtain support for two of them. *Id.* at 424.

88. *Id.* The two proposals included were: (1) amend the by-laws of the company to increase the number of directors by three persons. (2) creation of a shareholder committee for corporate responsibility. *Id.*

89. *Id.*

90. *Id.*

91. See, e.g., N.Y. Times, March 20, 1970 at 1, col. 5; Wall St. J., March 20, 1970, at 5, col. 1; Newsweek, April 27, 1970, at 109; Time, March 30, 1970, at 88.

92. The proposal for the shareholder committee received 2.73% of the votes cast. The proposal to amend the by-laws received 2.44% of the votes cast. Schwartz, *supra* note 33, at 430.

93. Propp, *supra* note 18, at 106. Prior to 1972, the Commission believed that resolutions were important enough to justify the interposition of federal substantive rules in place of vague state corporation law precepts, but they were not deemed to be an appropriate method for raising broader political questions about corporate decisions. *Id.*

94. 432 F.2d 659 (D.C. Cir. 1970), *vacated as moot*, 404 U.S. 403 (1971). The proposal submitted by the Medical Committee related to Dow Chemical's continuing produc-

of Appeals for the District of Columbia in *Medical Committee* objected to the Commission's position⁹⁵ that shareholder's proposals raising public policy concerns should be excluded from proxy materials.⁹⁶ The court held that a determination by the Commission is reviewable and accordingly remanded the case for further administrative proceedings within the proper limits of the Commission's discretionary authority.⁹⁷ The holding in *Medical Committee* appeared to be the product of judicial frustration with the Commission's inconsistent and conservative policies regarding shareholder access to corporate proxy machinery.⁹⁸

In response to judicial criticism, the Commission amended Rule 14a-8 in 1972.⁹⁹ The principal change was the elimination of the subjective inquiry into the shareholder proponent's motive as a relevant factor to consider in determining whether a proposal should be excluded.¹⁰⁰ Issuers could now omit proposals that "consist[ed] of a recommendation, request or mandate that action be taken with respect

tion and sale of napalm. Dow had argued, and the staff concurred, that the proposal was excludable since it related to the conduct of the issuers' ordinary business or, alternatively, was proposed primarily for the purpose of promoting a general political or social concern. *Id.* at 681. It is important to note this issue was reviewed by the Commission on appeal and that it had concurred with the staff's findings.

95. *Id.*

96. Propp, *supra* note 18, at 107.

97. 432 F.2d at 682. The court stated that "[w]e think that these provisions contain persuasive indicia that the Commission's proxy procedures are possessed of sufficient 'adversariness' and 'formality' to render its final proxy determinations amenable to judicial review" *Id.* at 670.

98. Schoenbaum, *Relationship Between Corporate Disclosure and Corporate Responsibility*, 40 *FORDHAM L. REV.* 590 (1972).

The clear impact of the language, legislative history and record of administration of section 14(a) is that its overriding purpose is to assure to corporate stockholders the ability to exercise their right — some could say their duty — to control the important decisions which affect them in their capacity as stockholders and owners of the corporation. . . . It could scarcely be argued that management is more qualified or more entitled to make these kinds of decisions than the shareholders who are the true beneficial owners of the corporation; and it seems equally implausible that an application of the proxy rules, which permitted such a result, could be harmonized with the philosophy of corporate democracy which Congress embodied in Section 14(a) of the Securities Exchange Act of 1934

432 F.2d at 681.

99. Securities Exchange Act of 1934 Release No. 9784 (Sept. 22, 1972), 37 Fed. Reg. 23,178 (1972).

100. Schwartz & Weiss, *supra* note 5, at 656. See *supra* notes 72 & 84 and accompanying text for some of the problems commonly associated with a subjective analysis of the proponents' motive.

to any matters, including a general economic, political, racial, religious, social or similar cause, that is not significantly related to the business of the issuer."¹⁰¹ Significantly, the Commission tacitly acknowledged that it is appropriate for shareholders to use the proxy process to raise social issues as long as there is a sufficient nexus¹⁰² between those issues and the business of the corporation.¹⁰³ As a result, the 1972 amendments to Rule 14a-8 gave rise to a dramatic increase in shareholder proposals on social issues while raising a host of new interpretive problems for the staff.¹⁰⁴ The Commission soon became concerned that given the increased requests for no-action letters by issuers, some shareholder proponents would misconstrue the holding in *Medical Committee* and attempt to appeal staff no-action determinations.¹⁰⁵

In 1974, the Court of Appeals for the District of Columbia held that a no-action determination by the staff is not appealable.¹⁰⁶ Such a staff determination does not constitute an order by the Commission.¹⁰⁷ The court also held that a Commission decision to

101. Release No. 9784, *supra* note 99.

... [T]he paragraph as amended provides for the omission of a proposal which are (sic) either not significantly related to the business of the issuer or not within its control. Proposals not within an issuer's control are those which are beyond its power to effectuate, and henceforth they may be omitted under this provision. The revised paragraph will apply to all proposals and will not be limited to those which involve general economic, political, racial, religious, social or similar causes. Also the provision is not intended to serve as a basis for the omission of traditional shareholder proposals dealing with stockholder relationships with management, such as cumulative voting, annual meetings and ratification of auditors, since these matters can be considered significantly related to the issuer's business or within its control.

Id.

102. The staff had developed an informal "one percent test" for determining when a proposal is significantly related to a issuer's business. *See, e.g.*, Letter to Libby-Owens Ford Co. dated Feb. 3, 1976 (proposal requesting the board of directors to provide a report to the stockholders concerning the company's compliance with the Arab countries' economic boycott of Israel).

103. STAFF REPORT, *supra* note 80, at 151. Schwartz & Weiss, *supra* note 5, at 654. The greatest challenge for the Commission was how to determine whether a proposal was significantly related to business to warrant inclusion in corporate proxy material. A second set of interpretive problems involved what evidence the staff should look to in determining whether a proposal deals with substantially the same subject matter. *Id.*

104. Schwartz & Weiss, *supra* note 5, at 657.

105. In its Supreme Court brief in *Medical Committee*, the Commission described the virtual chaos that it foresaw as blighting the administrative process if advisory opinions and enforcement decisions were reviewable in the Court of Appeals. Brief for the Petitioner at 45-48, SEC v. Medical Committee for Human Rights, 404 U.S. 403 (1972).

106. *Kixmiller v. SEC*, 492 F.2d 641 (D.C. Cir. 1974).

107. The court in *Kixmiller* stated:

decline review of a staff decision does not constitute a reviewable agency ruling.¹⁰⁸ While the decision did alleviate many of the Commission's concerns, growing corporate dissatisfaction with increasing shareholder proposals on a seemingly limitless number of subjects soon replaced these concerns.¹⁰⁹

In response to mounting corporate discontent and problems encountered in administering the shareholder proposal rule, the Commission made major revisions to Rule 14a-8 in 1976.¹¹⁰ One such revision was to reorganize Rule 14a-8 to enhance readability by grouping related provisions into four paragraphs.¹¹¹ The number of substantive grounds for exclusion of shareholder proposals was increased from four to thirteen.¹¹² The number of proposals which any one shareholder could submit was, for the first time, limited.¹¹³ The remaining parts of the 1976 amendments evidence the Commission's effort to prevent

Our authority to directly review Commission action springs solely from Section 25(a) of the Securities Exchange Act of 1934, which confines our jurisdiction to "order[s] issued by the Commission..." We think members of the Commission's staff, like staff personnel of other agencies, "have no authority individually or collectively to make 'orders,'" and that, on the contrary, "[o]nly the Commission makes orders." Here the Commission made no order on the merits of the petitioner's claim: rather, it emphatically "declined to review the staff's position."

492 F.2d at 643-44. *See also* National Automatic Laundry & Cleaning Council v. Schultz, 143 U.S. App. D.C. 274, 284-85, 443 F.2d 689, 699-700 (1972), wherein the Court of Appeals for the District of Columbia drew a clear line between opinions reflecting the definite views of an agency and the considerably less authoritative rulings by subordinate officials. *Id.*

108. 492 F.2d at 644. Now the Commission's practice is to decline review of staff no-action letters on shareholder proposals and thereby avoid appealability. Schwartz & Weiss, *supra* note 5, at 652.

109. These prompted a review by the Commission concentrating on corporate proposals to widen the scope of the recently revised "not significantly related to" exclusion and the "ordinary business" exclusion. Propp, *supra* note 18, at 108.

110. Securities Exchange Act of 1934 Release No. 34-12999 (Nov. 22, 1976), 41 Fed. Reg. 52,994 (1976).

111. *See infra* note 134.

112. The Commission's efforts at defining proper subjects are included in paragraph (C). The four prior grounds for exclusion remained. Five new grounds for exclusion were added: 1) proposals which would result in violation of state or federal law; 2) proposals that would result in violation of the proxy rules; 3) moot proposals; 4) proposals substantially identical to other proposals submitted in the same year; 5) proposals relating to specific dividend amounts. The other four grounds were merely a codification of previous staff interpretive positions now centralized in paragraph (C) as follows: 1) matters beyond the issuer's power to effectuate; 2) elections to office; 3) counter proposals to matters submitted by management; 4) proposals substantially identical to proposals submitted in a prior year. STAFF REPORT, *supra* note 80, at 151-52.

113. Release No. 34-12999, *supra* note 110. Prior to the 1976 amendments, shareholder proponents were entitled to submit an unlimited number of proposals. The statistics cited by the Commission in a release following the 1976 amendments indicated

abuse of the shareholder proposal process.¹¹⁴

As public corporations became more politicized, the staff's interpretation of the "significantly related" exclusion came under increasing criticism.¹¹⁵ The impetus for this criticism was a 1978 decision handed down by the United States Supreme Court in *First National Bank of Boston v. Bellotti*.¹¹⁶ The Court held that a Massachusetts state law limiting a corporation's capacity to make political contributions interferes with speech protected under the First Amendment.¹¹⁷ In so holding, the Court reasoned that, "[u]ltimately shareholders may decide through the procedures of corporate democracy, whether their corporation should engage in debate on public issues."¹¹⁸ By placing the responsibility for controlling corporate political expenditures on shareholders, *Bellotti* called into question the "significantly related" exclusion that the Commission had previously used to limit proposals on similar policy issues.¹¹⁹ Analogously, if a corporation could not be barred from speaking out on a political topic, the Commission should not refuse a shareholder the opportunity to express his views on a question of corporate policy with political overtones.¹²⁰ The Commission now had the task of squaring Rule 14a-8 with the *Bellotti* decision.

In 1980, the Senate Committee on Banking, Housing and Urban Affairs, in conjunction with the Commission, undertook an intensive

that the primary impact of this restriction would fall on proponents who seek to abuse Rule 14a-8. Securities Exchange Act Release No. 34-12598 (July 7, 1976), 41 Fed. Reg. 29,982 (1976).

114. Black & Sparks, *SEC Rule 14a-8: Some Changes in the Way the SEC Staff Interprets the Rule*, 11 U. Tol. L. Rev. 957, 964 (1980).

115. Karmel, *supra* note 14, at 12.

116. 435 U.S. 765 (1978). At issue in the case was a Massachusetts statute prohibiting corporations from making expenditures "for the purpose of . . . influencing or affecting the vote on any questions submitted to voters, other than one materially affecting any of the property, business or assets of the corporation." MASS. GEN. LAWS ANN. Ch. 55, § 8 (West Supp. 1983). In addition, the statute specified that no question submitted to voters solely concerning the taxation of income, property, or transactions of individuals should be deemed to materially affect the property, business or assets of the corporation. 435 U.S. at 768.

117. 435 U.S. at 795.

Such power in government to channel the expression of views is unacceptable under the First Amendment. Especially where, as here, the legislature's suppression of speech suggests an attempt to give one side of a debatable public question an advantage in expressing its views to the people, the First Amendment is plainly offended.

Id. at 785.

118. *Id.* at 794-95.

119. Propp, *supra* note 18, at 112.

120. *Id.* at 113.

study of corporate internal affairs which in part addressed the conflict between the *Bellotti* decision and Rule 14a-8.¹²¹ This study drew upon public hearings and comments received from several different groups, including corporations, law firms, financial institutions, public interest groups, academicians, and government officials.¹²² Although the report made several specific recommendations, it did not propose any major substantive changes to the shareholder proposal rule.¹²³ Specifically, the report suggested that the "significantly related" and "ordinary business" exclusions be examined in light of *Bellotti*.¹²⁴ Although the report was received favorably by the Commission,¹²⁵ recent Commission action signals an apparent retreat from some of the corporate accountability themes stressed in the report.¹²⁶

The most recent amendments adopted by the Commission¹²⁷ jeopardize the effectiveness of the shareholder proposal process. Many of the adopted changes will enable issuers to exclude shareholder proposals on a much easier basis than before.¹²⁸ Curiously, the Commission has adopted these changes despite strong feelings that the previous rule operated well.¹²⁹ The sweeping changes adopted by the Commission involve both procedural and substantive revisions.

III. SCOPE OF REVISIONS

Since its adoption in 1942,¹³⁰ the shareholder proposal rule has undergone a number of revisions¹³¹ generally directed at better defining and refining the basis for exclusion of such proposals from the proxy statement, as well as assuring the goals of shareholder

121. Steinberg, *The Securities Exchange Commission's Administrative Enforcement, and Legislative Programs and Policies—Their Influence on Corporate Internal Affairs*, 58 NOTRE DAME L. REV. 173, 185 (1982).

122. STAFF REPORT, *supra* note 80, at 29.

123. *Id.* at 29-30.

124. Steinberg, *supra* note 121, at 185.

125. *Id.* at 186.

126. Despite the report's recommendation, the Commission has yet to request comments on how to provide means of informing shareholders of corporate political activities and expenditures. Steinberg, *supra* note 121, at 184-90.

127. Release No. 34-20091, *supra* note 24, at 1-8.

128. Hudson, *SEC Proposes Rule Changes on Holders Votes*, Wall St. J., Oct. 15, 1982, at 3, col. 1.

129. Commissioner Evans defended the previous system, asserting that the shareholder proposal process, "is one of the trappings of corporate democracy, and we have to be careful not to snuff out that little light [of democracy]." *Id.*

130. See *supra* note 44 and accompanying text.

131. Including the most recent revision of Rule 14a-8, the rule has been revised seven times: (1) 1948, Release No. 4185, 13 Fed. Reg. 3973; (2) 1952, Release No. 4775, 17 Fed. Reg. 11,430; (3) 1954, Release No. 4979, 19 Fed. Reg. 246; (4) 1972, Release

communication.¹³² Currently, "[R]ule 14a-8 contains both the substantive standards which the Commission and its staff are called upon to interpret and enforce as well as a series of procedural rules designed to ensure that the staff is given adequate opportunity to perform its functions."¹³³ Rule 14a-8 is subdivided into five paragraphs,¹³⁴ four of which address the procedural rules for both the shareholder proponent and the issuer. The remaining paragraph deals solely with the substantive standards upon which management may rely in seeking to omit a shareholder proposal from its proxy statement.¹³⁵

Paragraphs (A) and (B) of Rule 14a-8 are concerned primarily with the eligibility of a shareholder proponent to rely on the shareholder proposal rule and the procedural requirements the proponent must follow in submitting his proposal.¹³⁶ Paragraphs (D) and (E) are largely devoted to the procedural requirements that confront an issuer when dealing with shareholder proposals.¹³⁷ Paragraph (C) sets forth thirteen substantive criteria¹³⁸ for omitting shareholder proposals from

No. 9874, 37 Fed. Reg. 23,178; (5) 1976, Release No. 34-12999, 41 Fed. Reg. 53,000; (6) 1978, Release No. 34-15384, 43 Fed. Reg. 58,522; (7) 1983, Release No. 34-20091, 47 Fed. Reg. 47,420.

132. SEC DOCKET, *supra* note 13, at 496.

133. Black & Sparks, *supra* note 30, at 8.

134. Paragraph (A) contains procedural requirements for shareholder proponents. Paragraph (B) governs shareholder proponents supporting statements. Paragraph (C) lists thirteen substantive grounds for exclusion of proposals. Paragraph (D) & (E) contain procedural requirements for issuers.

135. Black & Sparks, *supra* note 30, at 8.

136. SEC DOCKET, *supra* note 13, at 503.

137. *Id.* at 512.

138. Briefly stated, Rule 14a-8(C) says that the issuer may omit a proposal and any statement in support thereof from its proxy statement and form of proxy under any of the following circumstances: (1) If the proposal is, under the laws of the issuer's domicile, not a proper subject for action by security holders (2) If the proposal, if implemented, would require the issuer to violate any state law or federal law of the United States or any law of any foreign jurisdiction (3) If the proposal or supporting statement is contrary to the Commission's proxy rules and regulations (4) If the proposal relates to the redress of any personal claim or grievance (5) If the proposal relates to operations which account for less than 5% of the issuers' total assets . . . and is not otherwise significantly related to the issuers' business; (6) If the proposal deals with a matter beyond the issuers' power to effectuate; (7) If the proposal deals with matters relating to ordinary business operations of the issuer; (8) If the proposal relates to an election to office; (9) If the proposal is counter to a proposal to be submitted by the issuer at the meeting; (10) If the proposal has been rendered moot; (11) If the proposal is substantially duplicative of a proposal previously submitted to the issuer (12) If the proposal deals with substantially the same subject matter as a prior proposal . . . if submitted at one meeting and it received less than 5% of total votes cast, at two meetings and it received less than 8% of the votes cast, three or more meetings and it received less than 10% of votes cast

the issuer's proxy material.¹³⁹ The thirteen criteria contained in paragraph (C) are designed to permit exclusion from an issuer's proxy materials those proposals which are not proper for shareholder action or constitute an abuse of the shareholder proposal process.¹⁴⁰ In order to facilitate a better understanding of the present amendments to Rule 14a-8 it is necessary to address the procedural and substantive provisions separately.¹⁴¹

A. Procedural Revisions

The procedural revisions in the current amendments to the shareholder proposal rule are contained in the first four subsections of Rule 14a-8(A), the first two subsections of Rule 14a-8(B) and in Rule 14a-8(D).¹⁴² The Commission promulgated these procedural revisions with the hope of curbing the abuse of the shareholder proposal process and reducing disclosure burdens on the issuer.¹⁴³ Each of these changes will be examined in turn.

The present revisions to Rule 14a-8(A)(1) increase the stringency of the eligibility requirements necessary for a shareholder proponent to invoke the shareholder proposal process.¹⁴⁴ Prior to these revisions, a shareholder proponent only had to be a record or beneficial owner¹⁴⁵ of a security and continue to own such security through the date of the meeting.¹⁴⁶ A shareholder proponent must now satisfy both minimum investment¹⁴⁷ and holding period requirements¹⁴⁸ in order to submit a shareholder proposal.¹⁴⁹ The Commission believes that the present abuse can be curtailed by requiring shareholders who put the company and other shareholders to the expense of including a proposal in a proxy statement to have some measured economic stake or investment interest in the company.¹⁵⁰ Under the new provision

. . . . (13) If the proposal relates to a specific amount of cash or stock dividend. 17 C.F.R. § 240.14a-8(C) (1984). *Reprinted in* appendix.

139. SEC DOCKET, *supra* note 13, at 505.

140. *Id.* at 505-6.

141. The procedural requirements merely lay the groundwork for the substantive determination of the propriety of the proposal. Black & Sparks, *supra* note 30, at 961.

142. 17 C.F.R. § 240.14a-8 (1984). *Reprinted in* appendix.

143. SEC DOCKET, *supra* note 13, at 503.

144. Karmel, *supra* note 14, at 8.

145. A beneficial owner of a security is a person entitled to the economic enjoyment of a security, or who has the power to direct how the security will be voted or whether it will be sold. SOLOMON, *supra* note 6, at 460.

146. 17 C.F.R. § 240.14a-8(A)(1) (1984). *Reprinted in* appendix.

147. *See infra* note 151 and accompanying text. *See also infra* appendix.

148. *See infra* note 153 and accompanying text. *See also infra* appendix.

149. 17 C.F.R. § 240.14a-8(A)(1) (1984). *Reprinted in* appendix.

150. Release No. 34-20091, *supra* note 24. Presumably, these changes would serve

a shareholder proponent must own at least one percent or \$1,000 in market value¹⁵¹ of a security which entitles him to vote at the shareholders' meeting on his proposal.¹⁵² Also, a shareholder must have owned the securities for no less than one year prior to submission of his proposal.¹⁵³ Another indication of the more stringent eligibility requirements is the restriction on shareholder proponents who participate in additional proxy solicitations.¹⁵⁴ The Commission believes this revision is consistent with the goals of the Proxy Review Program by reducing disclosure costs for the issuer.¹⁵⁵

Under the most recent revisions, shareholders who submit written proxy material to a group with substantial security holdings are unable to have their proposals included in the issuer's proxy statements.¹⁵⁶ Previously, there was no restriction on shareholder proponents who participated in a separate proxy solicitation.¹⁵⁷ Rule 14a-8(A)(1) now precludes shareholder proponents who have already solicited or delivered written proxy materials to holders of more than twenty-five percent of the outstanding stock¹⁵⁸ from having their proposals included in the issuer's proxy material.¹⁵⁹ The rationale behind this revision is that when a proponent undertakes the cost of communicating with other shareholders, it is unnecessary to impose on an

to demonstrate some requisite long-term and substantial financial commitment to a corporation. Karmel, *supra* note 14, at 9.

151. Karmel, *supra* note 14, at 2. While a group may aggregate its holdings in order to meet the 1% or \$1000 investment requirement in 14a-8(A)(1), the group could only sponsor one shareholder proposal with the aggregated holdings. 247 CORP. PRAC. SERV. (BNA) (Aug. 23, 1983).

152. The securities are valued at \$1000 computed by use of the average of the bid and asked prices of such securities, as of the date within sixty days prior to the date of submission of the proposal. Release No. 34-20091, *supra* note 24, at 2.

153. 17 C.F.R. § 240.14a-8(A)(1) (1984). *Reprinted in* appendix. In the event the issuer includes the shareholder's proposal in its proxy soliciting material for the meeting and the shareholder proponent fails to comply with the requirement that he continuously hold such securities through the meeting date, the issuer shall not be required to include any proposals submitted by the proponent in its proxy material for any meeting held in the following two calendar years. *Id.*

154. 17 C.F.R. § 240.14a-8(A)(1)(II) (1984). *Reprinted in* appendix.

155. *See supra* note 13.

156. Release No. 34-20091, *supra* note 24, at 2.

157. 17 C.F.R. § 240.14a-8(A)(1) (1983).

158. Outstanding stock is stock issued and in the hands of the shareholders and as such, does not include treasury stock. BLACKS LAW DICTIONARY 1270 (Rev. 5th ed. 1979).

159. 17 C.F.R. § 240.14a-8(A)(1) (1984). *Reprinted in* appendix. In the event the issuer includes a shareholder's proposal in its proxy material and the proponent thereafter delivers written proxy materials to the holders of more than 25 percent of a class of the issuer's outstanding securities entitled to vote with respect to such meeting, the issuer shall not be required to include any proposal submitted by that proponent in its proxy soliciting materials for any meeting held in the following two calendar years. *Id.*

issuer and its shareholders the added costs that will result from inclusion of a shareholder proposal in the issuer's proxy material.¹⁶⁰

In an effort to streamline the proxy rules it administers, the Commission has adopted a revision to Rule 14a-8(A)(2). The shareholder proponent is no longer required to notify the issuer of his intention to appear personally at the shareholder meeting.¹⁶¹ The Commission believes that the old requirement¹⁶² served little purpose and only added incidental verbiage when included with the shareholder's proposal.¹⁶³ In conjunction with the deletion of the notice requirement,¹⁶⁴ a shareholder proponent is permitted to have any person who is authorized under applicable state law¹⁶⁵ present his proposal at the meeting.¹⁶⁶ This revision provides greater assurance that a proposal will actually be presented at the meeting by a well-informed person.¹⁶⁷

Under Rule 14a-8(A)(2), the shareholder proponent is now required to provide proof that he satisfies the minimum investment and holding period requirements when he submits his proposal.¹⁶⁸ Previously, this information had to be provided only if requested by management.¹⁶⁹ Also, the proponent had only to prove that he was a beneficial owner of a security¹⁷⁰ and that he owned such security through the date of the

160. SEC DOCKET, *supra* note 13, at 503.

161. *Id.*

162. 17 C.F.R. § 240.14a-8(A)(2) (1983). The shareholder proponent had to notify the issuer in writing at the time he submitted his proposal of his intention to appear personally at the meeting to present his proposal. *Id.*

163. *Summary of Comments*, *supra* note 19, at 38. See also Release No. 34-20091, *supra* note 24, at 2.

164. Release No. 34-20091, *supra* note 24, at 2.

165. SEC DOCKET, *supra* note 13, at 504. "The Commission continues to believe, however, that where state law permits a person other than a shareholder to act as proxy for a shareholder, such person should be permitted to present the proposal." Release No. 34-20091, *supra* note 24, at 2. "It must be emphasized, however, that it would continue to be the proponent's responsibility, not his representatives, to insure that the proposal is presented." SEC DOCKET, *supra* note 13, at 504.

In the event that the proponent or his representative fails, without good cause, to present the proposal for action at the meeting, the issuer shall not be required to include any proposals submitted by the proponent in its proxy soliciting material for any meeting held in the following two calendar years.

17 C.F.R. § 240.14a-8(A)(2) (1984). *Reprinted in* appendix.

166. SEC DOCKET, *supra* note 13, at 504.

167. *Id.* See *Summary of Comments*, *supra* note 19, at 39.

168. 17 C.F.R. § 240.14a-8(A)(2) (1984). *Reprinted in* appendix.

169. 17 C.F.R. § 240.14a-8(A)(1) (1983). "If the management requests documentary support for a proponent's claim that he is a beneficial owner of a voting security of the issuer, the proponent shall furnish appropriate documentation within ten business days after receiving the request." *Id.*

170. *Id.* See *supra* note 145.

meeting.¹⁷¹ Under the present revisions a shareholder must provide documentary support at the time he submits a proposal.¹⁷² This documentary support must include the shareholder's name, address, and number of the issuer's securities he holds of record or beneficially and the dates upon which he acquired such securities.¹⁷³ In addition, a shareholder must provide documentary support for any claim of beneficial ownership at the time he submits his proposal.¹⁷⁴ Finally, the Commission adopted an interpretive change which provides that attendance at another shareholder meeting will no longer be good cause for failure to present a proposal at a meeting.¹⁷⁵ The Commission concludes that this excuse is no longer valid since a shareholder can now appoint a representative to present his proposal at the meeting.¹⁷⁶ Taken collectively, the revisions to Rule 14a-8(A)(2) will eliminate some of the busy work for issuers and it should allow issuers to concentrate more on the issues addressed in shareholder proposals.

The issuer must have time to fully assess a shareholder's proposal before any benefits from the shareholder proposal process will be realized. As amended, Rule 14a-8(A)(3) extends the advance submission date by thirty days.¹⁷⁷ Now a shareholder proponent must submit his proposal for inclusion in the issuer's proxy materials 120 days before the filing of preliminary proxy materials by the issuer.¹⁷⁸ The Commission believes this change will benefit both the issuers¹⁷⁹ and shareholder proponents

171. *Id.*

172. 17 C.F.R. § 240.14a-8(A)(2) (1984). *Reprinted in* appendix.

173. Release No. 34-20091, *supra* note 24, at 2. *See also*, Letter to Atlas Corporation, dated July 26, 1968 for the previous staff interpretation.

174. Release No. 34-20091, *supra* note 24, at 2.

175. *Id.* *See also*, Letter to Atlas Corporation, dated July 26, 1968 (the staff held that attendance at another shareholder meeting was considered good cause for failure to present a proposal at a meeting). The Commission believes this position may be inconsistent with the provisions of the rule that are designed to assure that the proposal will be presented for action at the meeting. SEC DOCKET, *supra* note 13, at 504.

176. SEC DOCKET, *supra* note 13, at 504.

177. Release No. 34-20091, *supra* note 24, at 2.

178. 17 C.F.R. § 240.14a-8(A)(3)(I) (1984). *Reprinted in* appendix.

An exception to this rule occurs if no annual meeting was held in the previous year or the date of the annual meeting has been changed by more than 30 calendar days from the date contemplated at the time of the previous year's proxy statement. In this case, a proposal shall be received by the issuer a reasonable time before the solicitation is made.

Id.

179. Frequently, the issuers have as little as ten days between the last date for submission of proposals and the filing date specified in Rule 14a-8(D) for submitting objections to proposals. This limited period of time is proving inadequate for issuers to consider the security holder submissions and to prepare objections where appropriate.

SEC DOCKET, *supra* note 13, at 504.

by making the processing of no-action requests more efficient.¹⁸⁰ In addition, the increased number and complexity of shareholder proposals and longer time necessary for printing proxy materials justifies the increase.¹⁸¹ The Commission, recognizing the problems these changes may cause for issuers and shareholder proponents alike, has granted an additional six-month transition period before the revision of Rule 14a-8(A)(3) becomes effective.¹⁸² The increased amount of time for issuers to assess shareholder proposals under Rule 14a-8(A)(3) should help to decrease the disclosure burdens on issuers.

To further reduce disclosure burdens on issuers, the Commission has revised Rule 14a-8(A)(4) to reduce the maximum number of proposals a shareholder can submit from two to one.¹⁸³ The Commission believes this revision will not only reduce issuer costs, but will also improve the readability of the proxy statement.¹⁸⁴ Moreover, the Commission believes this will not substantially limit the ability of shareholder proponents to bring important issues before the shareholder body at large.¹⁸⁵ Theoretically, reducing the number of proposals from two to one will not prevent the shareholder proponent from addressing an important issue in the one proposal.

In an effort to allow shareholders a better opportunity to assess issues in their proposals, the Commission has amended Rule 14a-8(A)(4).¹⁸⁶ The Commission now requires inclusion of a shareholder's supporting statement in the issuer's proxy material even when the issuer chooses not to oppose the proposal.¹⁸⁷ Previously, if an issuer chose not to oppose the proposal, only the shareholder's proposal was required to be

180. "An increased number of proposals and reductions in the Commission Staff available to process contested security holder proposals have made it difficult for the staff to provide timely responses to issuers' letters submitted pursuant to Rule 14a-8(D)." *Id.*

181. *Id.*

182. "The Commission realizes that many shareholder proponents and issuers may be adversely affected unless there is a reasonably lengthy transition period prior to the effectiveness that will allow all interested persons adequate time to familiarize themselves with the requirements and to comply with those requirements." Release No. 34-20091, *supra* note 24, at 2.

. . . [W]hile all other amendments to Rule 14a-8 will be applicable to proposals submitted to issuers who file their preliminary proxy materials with the Commission on or after January 1, 1984, the effectiveness of the new timeliness deadlines set forth in paragraphs (A)(3) and (D) of the amended rule are deferred an additional six months . . . to July 1, 1984.

Id. at 3.

183. 17 C.F.R. § 240.14a-8(a)(4) (1984). *Reprinted in* appendix.

184. Release No. 34-20091, *supra* note 24, at 3.

185. *Id.*

186. *Id.*

187. 17 C.F.R. § 240.14a-8(B)(1) (1984). *See also* Release No. 34-20091, *supra* note 24, at 3. A supporting statement is included with the shareholder proposal to clarify and supplement the proposal and in some instances offer background information.

included in the issuer's proxy materials.¹⁸⁸ The Commission believes such supporting statements will provide shareholders with background information that may be helpful in considering the proposal.¹⁸⁹

The Commission also adopted a change in Rule 14a-8(B)(1) that provides greater flexibility to shareholders when drafting their proposals.¹⁹⁰ Shareholder proponents are now able to allocate the 500 word limit between the proposal and the supporting statement any way they see fit.¹⁹¹ This change should alleviate the artificial division of the shareholder proponent's argument between the proposal and the supporting statement.¹⁹² The revisions adopted in Rule 14a-8(B)(1) will provide shareholders with more information and greater flexibility without imposing any additional burden on the issuer or the staff.¹⁹³

The Commission revised Rule 14a-8(B)(2) to alleviate some of the present administrative problems and time constraints on the staff.¹⁹⁴ Previously, the staff was unable, in all cases, to respond timely to shareholder's requests for the name and address of any particular proponent.¹⁹⁵ The current revision provides that the Commission will no longer disclose the name and address of a shareholder proponent who is not identified in the issuer's proxy statement.¹⁹⁶ The Commission believes this will allow the staff to make more efficient and better use of its limited resources.¹⁹⁷ As a result, Rule 14a-8(B)(2) requires the name and address of a shareholder proponent to either be included in the proxy statement or be available upon request from the issuer.¹⁹⁸

188. 17 C.F.R. § 240.14a-8(B)(1) (1983).

189. Release No. 34-20091, *supra* note 24, at 3.

190. *Id.*

191. *Id.* See also, *Summary of Comments*, *supra* note 19, at 45. The previous limitation on a supporting statement was 200 words in support of the proposal. 17 C.F.R. § 240.14a-8(B)(1) (1983).

192. *Summary of Comments*, *supra* note 19, at 46. Several commentators argued that the previous requirement encouraged numerous "whereas" clauses that detracted from the readability of a proxy statement. *Id.*

193. *Id.* G.M. noted that the revision will probably result in longer proposals in general, but believed that the quality of submissions would increase. *Id.*

194. When proxy materials containing uncontested proposals are not reviewed by the staff in accordance with the Commission's selective review procedures, such materials are forwarded to the files before the request arrives. Reordering these materials for the purpose of ascertaining the names and addresses of proponents has in some instances proved to be time consuming.

SEC DOCKET, *supra* note 13, at 505.

195. *Id.*

196. Release No. 34-20091, *supra* note 24, at 3.

197. SEC DOCKET, *supra* note 13, at 505.

198. 17 C.F.R. § 240.14a-8(B)(2) (1984). *Reprinted in appendix.* It is important to note that Rule 14a-8(B)(2) does not require the issuer to include the shareholder's

Consistent with its effort to alleviate present time constraints on the staff, the Commission now requires an issuer to submit his intention to omit a shareholder proposal earlier.

In order to allow the staff to better assess an issuer's decision to omit a shareholder proposal, the Commission revised Rule 14a-8(D).¹⁹⁹ Previously an issuer was required to notify the Commission of its intention to omit a shareholder proposal²⁰⁰ at least fifty days prior to filing its preliminary proxy materials.²⁰¹ The revision increases the deadline for notification from fifty to sixty days²⁰² in advance of the filing date of preliminary proxy materials.²⁰³

The Commission has adopted this revision in conjunction with Rule 14a-8(A)(3), which provides for a thirty-day increase in the deadline for submitting shareholder proposals.²⁰⁴ Moreover, like the revision adopted in Rule 14a-8(A)(3),²⁰⁵ there will be a six-month transition period before Rule 14a-8(D) will become effective.²⁰⁶ This increased time allowed the staff under Rule 14a-8(D) should allow for a more thorough examination of the issuer's substantive reasons for omitting a shareholder proposal.

B. Substantive Revisions

The shareholder proposal rule enumerates thirteen grounds²⁰⁷ for omitting shareholder proposals from corporate proxy materials. This codifies over forty years of interpretation of the basic premise that stockholders are entitled to act only upon those proposals which are proper subjects for their consideration.²⁰⁸ The purpose of the thirteen subparagraphs is to balance the rights and responsibilities of a corporation's security holders, board of directors, and management.²⁰⁹ Each revision must be discussed with reference to those principles.

name and address in the corporate proxy materials, however, the issuer may do so at its sole discretion. Release No. 34-20091, *supra* note 24, at 3.

199. 17 C.F.R. § 240.14a-8(D) (1984). Reprinted in appendix.

200. See generally, § 240.14a-8(D) (1984). Reprinted in appendix.

201. 17 C.F.R. § 240.14a-8(D) (1983).

202. Release No. 34-20091, *supra* note 24, at 4. See *supra* note 182. "It should be noted that the sixty-day time frame is significantly shortened when the staff allows the shareholder proponent to amend his or her proposal to conform to the provisions of the rule before considering its substantive propriety." SEC DOCKET, *supra* note 13, at 504.

203. Release No. 34-20091, *supra* note 24, at 4.

204. *Id.* at 3, 4. Thus the new timeliness requirements will apply only to shareholder proposals submitted to issuers filing their preliminary proxy material on or after July 1, 1984. *Id.* at 2.

205. See *supra* note 178.

206. See *supra* note 182.

207. See *supra* note 138.

208. Black & Sparks, *supra* note 114, at 964.

209. Schwartz & Weiss, *supra* note 5, at 658.

The Commission revised Rule 14a-8(C)(1) to alleviate the staff's present perceived interpretive problems in administering this provision.²¹⁰ Traditionally, in applying the "proper subject" test,²¹¹ the staff made difficult and often subjective judgments about the meaning of state corporation statutes.²¹² Over the years, the staff has interpreted most proposals cast in the form of a recommendation or by-law amendment to be a "proper subject" for stockholder action.²¹³ Therefore, these interpretations have often turned on the form, rather than the substance, of the proposal.²¹⁴

The Commission adopted a change in Rule 14a-8(C)(1) to clarify any misconception issuers may have had concerning the staff's

210. Release No. 34-20091, *supra* note 24, at 3.

211. Black & Sparks, *supra* note 114, at 966. "While such statutory provisions point to the locus for decision-making, they do not purport to preclude stockholder action or to suggest that stockholders may not act in some areas." *Id.*

212. "Under this approach, the staff never inquired into the substantive nature of the proposed by-law and, as a result, even matters which were otherwise unquestionably within the exclusive domain of the directors were made subject to shareholder action." *Id.* See also, Eisenberg, *Current Applications of the Shareholder Proposal Rule*, 15 REV. SEC. REG. 905 (1982). *E.g.*, Letter to General Electric Company dated Jan. 27, 1982 (shareholder proposal requesting management to ban the use of cigarettes on company premises); Letter to Watkins-Johnson Company dated Feb. 3, 1982 (shareholder proposal requesting management to institute a dividend reinvestment plan).

213. That interpretation was based on the experience of the staff that generally under state corporation law a request for the board of directors to consider certain actions was deemed proper for shareholder action as it did not infringe upon the directors' statutory authority to manage the corporation. Release No. 34-20091, *supra* note 24, at 3. To reiterate what the Commission said in 1976:

[I]t is the Commission's understanding that the law of most states do not, for the most part, explicitly indicate those matters which are proper for security holders to act upon but instead provide only that "the business and affairs of every corporation organized under this law shall be managed by its board of directors," or words to that effect. Under such a statute, the board may be considered to have exclusive discretion in corporate matters, absent a specific provision to the contrary in the statute itself, or the corporation's charter or by-laws. Accordingly, proposals by security holders that mandate or direct the board to take certain action may constitute an unlawful intrusion on the board's discretionary authority under the typical statute. On the other hand, however, proposals that merely recommend or request that the board take certain action would not appear to be contrary to the typical state statute, since such proposals are merely advisory in nature and would not be binding on the board even if adopted by a majority of the security holders.

Release No. 34-12999, *supra* note 110, at 3.

214. Previously, the pertinent inquiry almost always concerned the form rather than the substance of the proposal; if the proposal is in the form of a recommendation, then the staff almost never authorized its omission under this exemption. Eisenberg,

application of the "proper subject" provision.²¹⁵ Specifically, the Commission revised the note accompanying Rule 14a-8(C)(1).²¹⁶ The revision reflects "an increased sensitivity by the staff to the fallacy inherent in the view that any proposal framed as a request or recommendation to the board of directors may be deemed a proper subject for stockholder action, regardless of the substantive content of that proposal."²¹⁷ The revision sets forth that state law governs the issue of whether the form of the proposal, recommendatory or mandatory, affects its inclusion in the issuer's proxy material.²¹⁸ The Commission believes the revision will give the "proper subject" provision more meaning and dispel any notion that the staff administers Rule 14a-8(C)(1) based solely on the form of the proposal.²¹⁹

The Commission has expanded the "personal grievance" exclusion²²⁰ to make this provision also emphasize the substance rather than the form of the proposal.²²¹ Previously, sophisticated shareholder proponents could avoid the exclusionary impact of Rule 14a-8(C)(4) by drafting their proposals in broad terms of general interest to other shareholders.²²² In so doing, a shareholder proponent purposely avoids using narrow terms which would reflect his personal interest in submitting the proposal.²²³ The present revision allows an issuer to omit a proposal if it is designed to result in a benefit to the shareholder proponent not shared with the other shareholders at large.²²⁴ The Com-

supra note 212, at 905.

215. Release No. 34-20091, *supra* note 24, at 3.

216. The Note was first added to Rule 14a-8 in 1976 to explain the staff's interpretive approach in considering the application of Rule 14a-8(C)(1). *Id.* "The Note, however, has been revised to make it clear that whether the nature of the proposal, mandatory or precatory, affects its includability is solely a matter of state law, and to dispel any mistaken impression that the Commission's application of paragraph (C)(1) is based on the form of the proposal." *Id.*

217. Black & Sparks, *supra* note 114, at 969. *See also*, Letter to Rorer Group, Inc. dated Feb. 5, 1980.

218. 17 C.F.R. § 240.14a-8(C)(1) (1984). *Reprinted in* appendix.

219. Release No. 34-20091, *supra* note 24, at 3.

220. *See generally*, 17 C.F.R. § 240.14a-8(C)(4), *Reprinted in* appendix.

221. *Summary of Comments*, *supra* note 19, at 58. The revised language is intended to conform the provision to the staff's present interpretive position and to assure that the shareholder proposal process is not being used by shareholders for personal reasons.

222. SEC DOCKET, *supra* note 13, at 507. Previously the staff interpreted Rule 14a-8(C)(4) very narrowly and required the issuer, in order to justify the application of the provision, to clearly demonstrate that the proposal under scrutiny relates to a personal claim or grievance. The staff determined that this requirement was met in those instances where the proposal or its supporting statement indicated on its face that a personal grievance existed, a rather formidable task in most instances. *Id.* at 506-507.

223. *Id.*

224. 17 C.F.R. § 240.14a-8(C)(4) (1984). *Reprinted in* appendix. However, the Commission's intent is not to exclude proposals relating to an issue in which a shareholder

mission believes the revision will conform to the present staff's interpretive position.²²⁵ In addition, the revision will prevent any further abuse by shareholder proponents attempting to achieve personal ends which are not necessarily in the common interests of the shareholders in general and may not be significantly related to the issuer's business.²²⁶

The Commission amended Rule 14a-8(C)(5) to establish objective standards with which issuers can determine when a proposal is not significantly related to its business.²²⁷ Previously, the Commission had attempted to develop an objective standard based on economic significance of the proposal to the issuer.²²⁸ However, this generated intense criticism and was never formally adopted.²²⁹ Although the Commission believes that a totally objective standard for determining the applicability of the "significantly related" provision is not feasible, the staff's previous interpretation unduly limited the effectiveness of the

is personally, intellectually or emotionally committed. Release No. 34-20091, *supra* note 24, at 4.

225. *Summary of Comments*, *supra* note 19, at 58. See Release No. 34-20091, *supra* note 24, at 4.

226. Release No. 34-20091, *supra* note 24, at 4. *But see*, the Federal Bar Association feared that the present revision would be applied to exclude proposals of special interest groups, such as religious organizations, where the proposal is not significantly related to the business of the issuer and is of interest to shareholders in general. *Summary of Comments*, *supra* note 19, at 61.

227. SEC DOCKET, *supra* note 13, at 507.

228. In interpreting prior versions of this provision, the Commission and its staff had attempted to establish a viable objective standard for determining the circumstances under which the subject matter of a proposal would be deemed significantly related. Eventually the staff agreed to the omission of proposals that constituted less than one percent of company sales, assets and earnings. SEC DOCKET, *supra* note 13, at 508. See e.g., Letter to American Home Products, dated May 4, 1975; Letter to International Business Machines Corporation, dated May 4, 1975 (the staff concurred with management in exclusion of proposals requesting reports on company policy regarding compliance with the Arab nations' economic boycott of Israel because their business with Arab countries constituted less than one percent of the company's sales, assets & earnings).

229. SEC DOCKET, *supra* note 13, at 508. The staff's interpretive position before 1976 was that a proposal which related to less than one percent of a company's overall business could be excluded under Rule 14a-8(C)(5). However, in 1976, the Commission decided not to codify the one percent economic test and stated:

In this regard, the Commission does not believe that (C)(5) should be hinged solely on the economic relativity of a proposal, since there are many instances in which the matter involved in a proposal is significant to an issuer's business, even though such significance is not apparent from an economic viewpoint. . . . And proposals relating to ethical issues such as political contributions also may be significant to the issuer's business, when viewed from a standpoint other than a purely economical one.

Release No. 34-12999, *supra* note 110.

exclusion.²³⁰ Consequently, Rule 14a-8(C)(5) now excludes shareholder proposals that do not affect at least five percent of a company's business²³¹ unless the proposal is otherwise significantly related to the issuer's business.²³² Thereby, the Commission codified the position that economic data is useful in determining the significance of a matter to the issuer's business.²³³ However, a proposal will not be excludable, notwithstanding its economic insignificance, if a significant relationship is demonstrated on the face of the resolution or supporting statement.²³⁴ The Commission believes a more objective standard will eliminate any future staff interpretive problems with Rule 14a-8(C)(5).²³⁵

The Commission adopted a significant interpretive change in administering the "ordinary business" exclusion. Under the previous staff interpretation, proposals submitted in the form of a request for a report²³⁶ were rarely excludable under Rule 14a-8(C)(7).²³⁷ Thus, shareholder proponents could easily circumvent the exclusionary impact of this provision.²³⁸ Requiring issuers to include proposals solely because those proposals are submitted in the form of a request for a report had caused the staff to lose sight of the purpose of the "ordinary business" exclusion.²³⁹ According to many critics, the

230. SEC DOCKET, *supra* note 13, at 509.

231. 17 C.F.R. § 240.14a-8(C)(5) (1984). *Reprinted in* appendix.

232. *Id.*

233. SEC DOCKET, *supra* note 13, at 509.

234. *Id.* Historically, the staff has taken the position that certain proposals, while relating to only a small portion of the issuer's operations, raise policy issues of significance to the issuer's business. Note, however, that when the proposal relates to an area in which the issuer has no involvement, the proposal is excludable under Rule 14a-8(C)(5). *Id. See, e.g.,* Letters to Long Island Lighting Company, dated Feb. 11, 1980 (cease further development, planning and construction of nuclear power plants); Owens Illinois Inc., dated Feb. 15, 1980 (liquidate the assets of the company that are located in the Republic of South Africa); and American Home Products Corporation, dated Feb. 13, 1978 (changes in the company's marketing and distribution of infant formula products). Where a significant relationship is not apparent on the face of the shareholder's proposal, the shareholder, as in the past, could demonstrate the relationship supplementally. SEC DOCKET, *supra* note 13, at 509.

235. SEC DOCKET, *supra* note 13, at 508.

236. Shareholders would request that the issuer prepare and disseminate a report to shareholders or a recommendation that a special committee be formed to examine a particular area of the issuer's business. *Id.* at 510.

237. Release No. 34-20091, *supra* note 24, at 4.

238. *Summary of Comments*, *supra* note 19, at 67.

239. *Id.* The policy behind this provision is to confine the solution of ordinary business problems to the board of directors and place such problems beyond the competence and direction of the shareholders. It is manifestly impracticable in most cases for stockholders to decide management problems at corporate meetings. SEC DOCKET, *supra* note 13, at 509.

previous staff interpretation elevated form over substance and effectively rendered the "ordinary business" exclusion a nullity.²⁴⁰ Experience shows that "[w]hile the search for objective standards is understandable, a standard which ignores the substance of the proposal is hardly desirable."²⁴¹ Under the present revision, the staff will consider whether the subject matter of the requested special report involves a matter of ordinary business;²⁴² where it does, the proposal will be omitted from the issuer's proxy materials.²⁴³

The Commission has also revised Rule 14a-8(C)(10) to concentrate primarily on the substance of the shareholder's proposal.²⁴⁴ Prior to the revision, issuers had to include shareholder proposals in their proxy materials regardless of whether the proposal was already substantially implemented;²⁴⁵ to require inclusion of such proposals only fills the proxy statement with irrelevant proposals.²⁴⁶ In the Commission's view, shareholders and issuers alike will be better served by an interpretation of Rule 14a-8(C)(10) that focuses on the overall substance of the proposal and not on a particular detail.²⁴⁷ Rule 14a-8(C)(10) will now permit the omission of a shareholder proposal "substantially implemented by the issuer."²⁴⁸ The Commission concedes

240. Release No. 34-20091, *supra* note 24, at 4. See, e.g., Letters to Westinghouse Electric Corp., dated Feb. 3, 1982 (report on implications on the sale of nuclear reactors); Westinghouse Electric Corp., dated Feb. 3, 1982 (report on equal employment and affirmative action efforts); General Electric Company, dated Feb. 3, 1982 (information about plant closings); Pacific Gas & Electric Company, dated Jan. 26, 1982 (report on storage of nuclear wastes); The General Tire & Rubber Company, dated Jan. 15, 1982 (disclosure of organizations to which the company makes contributions).

241. Black & Sparks, *supra* note 114, at 974-75.

242. Release No. 34-20091, *supra* note 24, at 4.

243. *Id.*

244. *Summary of Comments*, *supra* note 19, at 70.

245. Eisenberg, *supra* note 212, at 912. Previously the staff granted no-action requests pursuant to Rule 14a-8(C)(10) only in those circumstances where the action requested by the proposal, was already "fully" complied with. As a result of this interpretation, shareholders have argued successfully on numerous occasions that a proposal may not be excluded as moot, in cases where the company took most but not all of the actions requested by the proposal, because the proposal was not "fully" complied with. SEC DOCKET, *supra* note 13, at 510.

246. *Id.*

247. *Summary of Comments*, *supra* note 19, at 70. Hence, "[w]here management has in fact done all that a shareholder proposal seeks, it seems clear that the better result is not to muddy the proxy statements with a wholly irrelevant proposal." Eisenberg, *supra* note 212, at 912.

248. Release No. 34-20091, *supra* note 24, at 4. Whether a proposal is moot will still involve a factual determination on a case by case basis. SEC DOCKET, *supra* note 13, at 510.

that the new interpretive position will add subjectivity to the application of Rule 14a-8(C)(10).²⁴⁹ However, the Commission believes that the staff's previous formalistic application of Rule 14a-8(C)(10) only defeated the purpose of this exclusion.²⁵⁰

To better effectuate the overall objective of Rule 14a-8(C)(12), the Commission will no longer require inclusion of proposals concerned with substantially the same subject matter as proposals submitted in prior years. In the past, the staff allowed relatively minor changes in the scope or effect of a proposal to take the proposal outside the Rule 14a-8(C)(12) exclusion.²⁵¹ The present revision to Rule 14a-8(C)(12) allows issuers to exclude proposals dealing with substantially the same subject matter as a proposal submitted in prior years.²⁵² The proposal may be omitted from the issuer's proxy materials relating to any meeting of shareholders held within three calendar years after the last similar proposal was submitted.²⁵³ According to the Commission, this change is necessary to signal a clean break from the strict interpretive position the staff applied to the previous provision.²⁵⁴

Consistent with this change in attitude, the Commission has raised the minimum percentage of votes required for resubmission of proposals in subsequent years. In the past, Rule 14a-8(C)(12) required a three percent vote the first time a proposal was included, six percent the second time a proposal was voted upon, and ten percent every year thereafter.²⁵⁵ Under the present revision, the minimum percentage tests are increased to five percent and eight percent in the first and second years respectively, with the final test remaining at ten percent.²⁵⁶ The Commission believes that given the increased activities

249. Release No. 34-20091, *supra* note 24, at 4.

250. *Id.*

251. SEC DOCKET, *supra* note 13, at 511. Critics of the staff's previous interpretation argue that shareholders are able to evade the strictures of this provision by simply recasting the form of the proposal, expanding its coverage, or by otherwise changing its language so it is not identical to a prior proposal. *Id.* For example, a proposal that a company both terminate its operations in South Africa and make no new contracts in South Africa was not, in the staff's view, substantially the same as a proposal that the company make no new contracts in South Africa. See Letter to International Business Machines Corporation, dated Feb. 3, 1982.

252. 17 C.F.R. § 240.14a-8(C)(12) (1984). Reprinted in appendix.

253. *Id.*

254. Release No. 34-20091, *supra* note 24, at 4.

255. 17 C.F.R. § 240.14a-8(C)(12) (1983). Many issuers felt that they were continually bearing the cost of including shareholder proposals that had generated little interest when previously included in the proxy materials. *Summary of Comments, supra* note 19, at 75.

256. 17 C.F.R. § 240.14a-8(C)(12) (1984). Reprinted in appendix.

of institutional investors²⁵⁷ with respect to shareholder proposals,²⁵⁸ this revision will not substantially restrict a shareholder's access to the issuer's proxy machinery.²⁵⁹ This increased voting activity should, the Commission believes, allow greater potential support for shareholders' proposals.²⁶⁰ This revision is typical of the Commission's commitment to curtailing the alleged abuse of the shareholder proposal rule.

Overall, the Commission has substantially revised the shareholder proposal rule. These revisions represent a fundamental re-examination of the shareholder proposal rule in accordance with the Proxy Review Program.²⁶¹ The Proxy Review Program is designed to reduce disclosure burdens, streamline requirements and promote proxy readability.²⁶² A meaningful distinction of these revisions should be drawn, however, between those provisions imposing procedural requirements on the parties involved and those relating to the substantive exclusions embodied in the shareholder proposal rule. Many of the revisions to Rule 14a-8 have significant implications on a shareholder's ability to influence corporate actions by use of the issuer's proxy material.

IV. AN ASSESSMENT OF THE CURRENT REVISIONS TO RULE 14a-8

Individually, the revisions adopted by the Commission appear innocuous, but collectively they will be overly restrictive on the shareholder's ability to use the issuer's proxy machinery.²⁶³ The Commission appears to have lost sight of the intended purpose of Rule 14a-8.²⁶⁴ More importantly, the Commission has misinterpreted the present need for revisions to Rule 14a-8.²⁶⁵ The Commission contends that Rule 14a-8, as amended, "provides a fair and efficient mechanism for

257. Institutional investors include trust departments of commercial banks, insurance companies, large registered investment company complexes, self administered portfolios belonging to the largest corporate employee benefit plans, and educational endowments and foundations.

258. Release No. 34-20091, *supra* note 24, at 4. *But see*, M. EISENBERG, *supra* note 7, at 56-58.

259. Release No. 34-20091, *supra* note 24, at 4.

260. *Id.*

261. Karmel, *supra* note 14, at 5.

262. SEC DOCKET, *supra* note 13, at 496.

263. Lydenberg, *supra* note 16, at 64.

264. Congress created the Commission in 1934 to oversee and protect the basic rights of shareholders, including the right to vote on issues of vital corporate interest. The Commission cited cost cutting for government and industry as its motives in proposing to radically revamp the shareholder proposal system. Lydenberg, *supra* note 16, at 64.

265. The Commission initially considered three specific alternative proposals and invited comment on each alternative. The three proposals are part of the Commission's

the security holder process;"²⁶⁶ when in actuality, the changes make it considerably more difficult to achieve "fair corporate suffrage."

A. 14a-8(A)(1): Eligibility Requirements

The revisions adopted by the Commission to Rule 14a-8(A)(1) are largely unnecessary and over-inclusive. First, this provision requires that a shareholder proponent own \$1,000 or one percent of stock for one year to avail himself of the shareholder proposal process.²⁶⁷ These requirements discriminate against small or recent investors.²⁶⁸ Further, satisfaction of the minimum investment and holding period requirements is not dispositive of the legitimacy of a shareholder's proposal;²⁶⁹ the imposition of a refundable submission fee bears a more logical relationship to legitimacy of a shareholder's proposal. Such a fee would be fully refundable if a shareholder's proposal is later included in the issuer's proxy statement. Second, Rule 14a-8(A)(1) now states that shareholder proponents who participate in an additional

Proxy Review Program designed to reduce the burdens of compliance with the Commission's proxy rules consistent with investor protection. The three proposals are as follows: 1) would retain the current framework of Rule 14a-8 but incorporate certain revisions to specific provisions, several interpretations thereunder and staff practices in administering the rule.

2) would permit the issuer, with the approval of its security holders, to vary the procedures specified in the Commission's security holder proposal rule, subject to certain minimum standards prescribed by the Commission.

3) based on the premise that security holders should have relatively unfettered access to an issuers proxy statement. A numerical limit would be placed on the aggregate number of proposals required to be included in any proxy statement. 397 letters of comment were received from 383 commentators. 115 commentators supported proposal 1, while 145 commentators suggested that there should be no change in the existing rule. Twenty-four commentators expressed support for proposal 2. Only six commentators favored the adoption of proposal 3. Release No. 34-20091, *supra* note 24, at 1 (emphasis added). See also, *Summary of Comments*, *supra* note 19, at 7.

266. Release No. 34-20091, *supra* note 24, at 2.

267. 17 C.F.R. § 240.14a-8(A)(1) (1984). Reprinted in appendix. See also notes 144-153 and accompanying text.

268. Karmel, *supra* note 14, at 9. See also, *Summary of Comments*, *supra* note 19, at 34. Many commentators expressed the view that such eligibility requirements would create two classes of stockholders, large and small. In addition, this may have a discouraging effect on the already disenfranchised small investor who may wish to challenge management. *Id.* at 35.

269. STAFF REPORT, *supra* note 80, at 180. This may prevent small or temporary stockholders from presenting a proposal that is both lawful and appropriate. Karmel, *supra* note 14, at 9. Further "the staff's own examination has produced little support for the rationale that a reasonable 'minimum eligibility' requirement would eliminate a substantial portion of the proposals, or, more importantly, that it would distinguish between those which were offered in good faith and those which were frivolous or abusive." STAFF REPORT, *supra* note 80, at 123.

proxy solicitation involving a large number of shareholders are ineligible to have their proposals included in the issuer's proxy material.²⁷⁰ However, this provision fails to take into account the relationship between the subject matters addressed in each proxy solicitation. Collectively, the new eligibility requirements will unnecessarily restrain shareholder proponents with legitimate proposals from bringing them before their fellow shareholders.

1. Minimum Investment and Holding Period Requirements

The revised minimum investment and holding period requirements of Rule 14a-8(A)(1)²⁷¹ fail to eliminate from the ranks of shareholder proponents, activists who have in the past used the shareholder proposal process as a publicity mechanism to further their personal and political interests.²⁷² The new investment and holding period requirements theoretically forces shareholder proponents to demonstrate a long term and substantial financial commitment to the issuer.²⁷³ Unfortunately, this may allow an issuer to avoid addressing the merits of a shareholder proposal regardless of whether it is a valid subject for shareholder action under Rule 14a-8. Thus a shareholder's proposal is arbitrarily excluded from an issuer's proxy material even though the proposal may be both appropriate and proper under the applicable state corporation law.

Significantly, the Senate Committee on Banking, Housing and Urban Affairs as recently as 1980 concluded that "there is no significant evidence showing that satisfaction of a holding period or minimum investment requirement is indicative of legitimate or abusive proposals."²⁷⁴ In fact, the Commission, in rejecting similar eligibility requirements in 1976, noted that "the current eligibility requirements have been in operation for many years and generally have not been abused."²⁷⁵ The Commission, moreover, has not sufficiently demonstrated that the present eligibility requirements are being abused.²⁷⁶

270. 17 C.F.R. § 240.14a-8(A)(1). Reprinted in appendix. See *supra* notes 156-60 and accompanying text.

271. To be eligible to submit a proposal, a shareholder must own at least 1% or \$1000 in market value and have held such securities for no less than one year prior to the date on which he submits the proposal. Release No. 34-20091, *supra* note 24, at 2. See *supra* notes 151-53 and accompanying text.

272. Karmel, *supra* note 14, at 9.

273. Release No. 34-20091, *supra* note 24, at 2.

274. STAFF REPORT, *supra* note 80, at 180.

275. *Id.*

276. Commissioner Longstreth stated that:

The Commission misinterprets the need for the present revisions to the eligibility requirements.²⁷⁷ From 1981 to 1982, the total number of shareholder proposals submitted to issuers decreased from 991 to 850, a difference of 141.²⁷⁸ In addition, seventy-six fewer companies received shareholder proposals pursuant to Rule 14a-8 during that period, a decrease of nearly twenty six percent.²⁷⁹ More significantly, the number of staff no-action letters²⁸⁰ given when compared to the number of contested proposals²⁸¹ decreased by ten percent in the same period.²⁸² The interpretive changes adopted in the most recent amendments to Rule 14a-8 suggest that the staff, in the Commission's view, may be administering the shareholder proposal rule too loosely. However, an equally valid inference that can be drawn from these figures is that the issuers may themselves be abusing the shareholder proposal process by submitting frivolous requests for no-action letters.²⁸³ Further, the practical difficulties inherent in the revised minimum investment and holding period requirements outweigh many of their benefits.

Ascertaining whether the minimum investment requirement is met is laden with problems. Specifically, eligibility may be determined as either a product of market performance of the stock or by the capital needs of a particular company.²⁸⁴ If a company makes substantial use of equity financing²⁸⁵ or a prolonged decrease in the market

With minor exceptions, Rule 14a-8 in its present form has been in effect since 1976. The seven year record provides a strong case for continuing the Rule essentially as it is. . . . Moreover, each time we change a rule, we impose on the community of affected businessmen, investors and professionals the cost of having to master the changes.

Release No. 34-20091, *supra* note 24, at 7.

277. See *infra* notes 278-84 and accompanying text.

278. SEC DOCKET, *supra* note 13, at 501.

279. Typically the issuers receiving proposals are the larger and more widely followed corporations in the country. *Id.*

280. See *supra* note 63.

281. Contested proposals are simply shareholder proposals that management chooses to oppose and seek a staff no-action determination.

282. SEC DOCKET, *supra* note 13, at 501. The amount of contested proposals in 1981 was 387 while no-action letters issued by the Division of Corporation Finance totaled 285 or approximately 74%. In 1982 there were 487 contested proposals and only 313 no-action letters issued by the Division of Corporation Finance, or approximately 64%.

283. Despite the fact that shareholder proponents submitted 141 less proposals in 1982, the amount of contested proposals increased by 100 for the same time period. In addition, the percentage of no-action letters when compared to number of proposals decreased by 10% in 1982. Arguably, this is persuasive evidence that issuers are themselves currently abusing the shareholder proposal process.

284. *Summary of Comments*, *supra* note 19, at 35.

285. Equity financing means financing through the sale of shares of stock which

price of the stock occurs, then a shareholder could suddenly become ineligible to submit a proposal.²⁸⁶ Therefore, a small shareholder with a relatively stable investment may suddenly become ineligible to submit a proposal.²⁸⁷

The Commission plans to alleviate this problem by use of the average of the bid and asked prices method.²⁸⁸ However, this will fail to completely compensate for market fluctuations because the average of the bid and asked prices computation will only compensate for short term market fluctuations and not for prolonged market decreases.²⁸⁹ Moreover, this method cannot accommodate a dilution of the shareholder's percentage of ownership due to the substantial use of equity financing by the issuer.²⁹⁰ The result is that access to the issuer's proxy materials may be effectively precluded because a shareholder will fail to satisfy the minimum investment requirement. This was hardly the Commission's intent when Rule 14a-8 was originally promulgated.²⁹¹

The Commission has attempted to neutralize this effect by allowing shareholders to aggregate their holdings in order to satisfy the minimum investment requirement.²⁹² This, however, is an empty

increases the amount of shares outstanding. If this increase in shares outstanding is significant, this may effect the computation of the minimum investment requirement regarding percentage of ownership.

286. In either case there is a possibility that the shareholder's percentage of shares owned or market value of those shares will fall below minimum investment requirements and he will then be ineligible to submit a shareholder proposal.

287. A shareholder with a small stable investment faces a real possibility of becoming ineligible to submit a proposal despite the fact that the shareholder has made a good faith attempt to comply with the eligibility requirements. *Summary of Comments, supra* note 19, at 35.

288. Release No. 34-20091, *supra* note 24, at 2. The bid price is that which dealers are currently offering to buy the security for. The asked price is that which dealers are currently offering to sell the security for. K. SMITH & D. EITEMAN, *ESSENTIALS OF INVESTING* 77-78 (1974). Quotations of such bid and asked prices for an over-the-counter stock may be secured through stockbrokers who can obtain information through a computerized network that furnishes continuous quotations or through printed sheets that are revised daily. SOLOMON, *supra* note 6, at 803.

289. The use of averaging can only eliminate the effects of short term fluctuations and cannot really accommodate for prolonged market decreases.

290. The use of the average of the bid and asked prices method does not use shareholdings in the computation. As a result, it will be unable to compensate for a substantial increase in the amount of stock outstanding. A single extreme value, such as a prolonged decrease in the value of the stock, can effect the average to such an extent that it is debatable whether it is really representative or typical of the data. J. FREUND, *MODERN ELEMENTARY STATISTICS* 36 (4th Ed. 1972).

291. See *supra* note 12 and accompanying text.

292. Release No. 34-20091, *supra* note 24, at 2. See *supra* note 151.

gesture and will benefit few, if any, shareholders.²⁹³ Shareholders are frequently geographically dispersed and their only contact with the company is through management's proxy solicitation.²⁹⁴ Furthermore, since shareholder lists²⁹⁵ are seldom made public, many shareholders are unaware of the identity of other shareholders.²⁹⁶ These facts make it highly unlikely that shareholders will be able to contact each other in order to aggregate their shareholdings. Consequently, allowing shareholders to aggregate their shareholdings to meet the minimum investment requirement will not lessen the hardship of the new eligibility requirements.

The minimum holding period requirement creates substantial hardships on shareholder proponents without hardly any corresponding benefit to the shareholder proposal process.²⁹⁷ No logical relationship exists between the length of time a shareholder holds his stock and the amount of support a shareholder proposal can generate.²⁹⁸ The relevant inquiry is not the length of time the shares have been held, but rather the issue which the proposal addresses.²⁹⁹ A minimum holding period requirement would exclude certain shareholder proposals without regard to the welfare of the corporation;³⁰⁰ therefore, the duration of ownership should not be one of the requirements for a shareholder to submit proposals.

In sum, to preclude submission of a shareholder proposal based

293. See *infra* notes 294-96 and accompanying text.

294. Elliot, *supra* note 27, at 68.

295. Shareholder lists are a compilation of the names and addresses of the shareholders. The availability of a shareholder list is a question of state rather than federal law. Schwartz, *supra* note 33, at 491-92. Many state inspection statutes impose limitations on the right of inspection, especially as to persons eligible to assert the right and as to specific records subject to inspection. SOLOMON, *supra* note 6, at 296.

296. Schwartz, *supra* note 33, at 491.

297. See *infra* notes 346-49 and accompanying text.

298. STAFF REPORT, *supra* note 80, at 181. "On the subject of the minimum holding period, the staff has no comprehensive data available on the period for which proponents have held their stock, or, more important, on the correlation, if any, between the holding period and the likelihood the shareholder is 'abusing' the proposal process." *Id.* at 184.

299. *Summary of Comments*, *supra* note 19, at 33.

300. STAFF REPORT, *supra* note 80, at 183. A dramatic example of the lack of correlation between shareholdings and the ultimate success of a shareholder proposal was a proposal to Detroit Edison recommending that the company meet its energy needs by methods other than nuclear power, until questions regarding public safety and economics were solved. Despite the fact that the shareholder proponent only held six shares of stock, the proposal received 10.16% support. *The 1979 Proxy Season: How Institutions Voted on Shareholder Resolutions and Management Proposals*, prepared by the Investor Responsibility Research Center, Inc. (cited in STAFF REPORT, *supra* note 80, at 182).

on a minimum investment and holding period requirement is too restrictive given the lack of justification. Specifically, the revised eligibility requirements will restrict access to the corporate proxy machinery for small or recent shareholders. No logical relationship exists between small or recent shareholders and the present abuses of the shareholder proposal process.³⁰¹ Also, many shareholder activists who abuse the shareholder proposal process are well financed and frequently satisfy the revised eligibility requirements.³⁰² A more reasonable approach is to direct any deterrent provision at the group most likely to be responsible for the present abuse.

Imposing a fee on shareholders whose proposals are subsequently excluded from the issuer's proxy statement is a more appropriate deterrent to the present abuses of Rule 14a-8. The advantage of this method is that a more direct relationship exists between those shareholders whose fee is not refunded and those shareholders who are currently abusing the shareholder proposal process. A fee would deter professional stockholder activists and discourage frivolous proposals as well as the revised eligibility requirements will.³⁰³ However, the imposition of a fee would not arbitrarily exclude a shareholder proposal without considering its merits, as is ultimately done under the revised eligibility requirements.³⁰⁴ Also, a fee would arbitrarily not exclude those proposals that are appropriate under applicable state law.³⁰⁵

Under this proposed revision, each shareholder proponent would be assessed a \$100 refundable fee for each proposal submitted.³⁰⁶ Those shareholders who submit proposals which are either not opposed from

301. STAFF REPORT, *supra* note 80, at 183.

302. *Id.* at 181.

303. Only shareholders who submit proposals that are later excluded from the issuer's proxy statements bear the burden of the fee. Further, the fee would probably encourage more careful drafting of the proposals.

304. Under Rule 14a-8(A)(1), if a shareholder fails to meet the minimum investment and holding period requirements, then the proposal is excluded regardless of its merits. This is an arbitrary ban on proposals submitted by small or recent investors. However, with a submission fee, any shareholder who is legitimately interested in submitting a proposal can do so if he chooses.

305. A fee is only assessed on those proposals subsequently not deemed a proper subject for shareholder action under Rule 14a-8 and ultimately excluded from the issuer's proxy statement.

306. Each shareholder proponent pays the fee when he submits his proposal and only if the proposal is later included in the proxy statement will the fee be fully refunded. The \$100 figure was the one most commonly preferred by commentators who responded to this issue. See, *Summary of Comments*, *supra* note 19, at 54.

the start or later deemed appropriate for inclusion in the issuer's proxy materials³⁰⁷ would be refunded their fee. The imposition of a fee would deter frivolous proposals as well as encourage careful drafting of each proposal.

Imposing a fee on shareholder proponents is, however, not without its problems. Theoretically, imposing a fee would be a heavier burden on small investors.³⁰⁸ Also, given the substantive tightening up of the recent amendments to Rule 14a-8, the risk of non-inclusion of a shareholder's proposal may minimally deter legitimate proposals. However, a small shareholder would not face a total inability to submit a proposal as he will in the case of the revised minimum investment and holding period requirements.³⁰⁹ Also, a small or recent shareholder who wishes to gain access to the issuer's proxy machinery would have his \$100 submission fee fully refunded if his proposal were later included in the issuer's proxy statement. Imposition of a fee would, as a result, be more consistent with the policy of "fair corporate suffrage."³¹⁰ Furthermore, the imposition of a fee on those shareholders whose proposals are later excluded from the issuer's proxy materials acts as a formidable deterrent but is not overinclusive as are the revised eligibility requirements.

The imposition of a fee on shareholder proponents would ensure that any legitimately interested shareholder would not be arbitrarily precluded from participating in the shareholder proposal process.³¹¹ Specifically, imposing a fee on shareholder proponents would not discriminate against small or recent shareholders; every shareholder proponent who submits a proposal, whether a large or small investor, will be assessed a \$100 fee when he submits his proposal. However, those shareholders whose proposals are later included in the issuer's proxy materials will have their shareholder proposal submission fee fully refunded. As a result, those shareholder proponents who abuse

307. If the issuer does not oppose the proposal when it is submitted, then the shareholder proponent is refunded his fee. If the staff refuses to issue a no-action letter and the proposal is later included in the issuer's proxy material, that the fee will also be fully refunded.

308. The \$100 submission fee may prevent some small shareholders from submitting a proposal. However, this alternative will allow those shareholders who are legitimately interested, enough to pay the submission fee, to have management address the merits of their proposals.

309. See *supra* note 304.

310. With the shareholder submission fee there is no arbitrary restriction on access to the corporate proxy machinery. Small or recent shareholders would be treated the same as other shareholders.

311. See *supra* note 304.

the shareholder proposal process will bear the burden of the fee instead of subjecting innocent shareholder proponents to arbitrary eligibility requirements.

2. Participation in Additional Proxy Solicitation.

The exclusion of shareholder proposals based solely on a shareholder proponent's participation in an additional proxy solicitation is overinclusive.³¹² This revision will further exacerbate the inequities that now exist between issuers and shareholders.³¹³ A shareholder's proposal is frequently overwhelmed in an issuer's proxy material, since management has no length restrictions imposed on them when rebutting a shareholder proposal.³¹⁴ In addition, the exclusion of a proposal when there is no logical nexus³¹⁵ between the subject matter of the proposal and that of the additional proxy solicitation is arbitrary and unreasonably restrictive.

Significantly, Rule 14a-8(A)(1) fails to specify whether any connection is needed between the subject matter addressed in the additional proxy solicitation and that of the shareholder's proposal.³¹⁶ Unless there is a connection, there are arguably no duplicative costs imposed on the issuer and its shareholders.³¹⁷ Arbitrary exclusion of a shareholder's proposal under this provision may significantly decrease the amount of pertinent information available to shareholders in formulating an intelligent vote. Without this information supplied by the proposals, the shareholders will have insufficient knowledge of the manner in which their interests are being served.

To alleviate this problem, Rule 14a-8(A)(1) should only exclude a shareholder's proposal if it involves the same subject matter as the other proxy solicitation. To require inclusion of proposals involving the same subject matter only imposes on the issuer and its

312. See *infra* note 316-17 and accompanying text.

313. *Summary of Comments*, *supra* note 19, at 37.

314. *Id.*

315. If the subject matters are not related, then allowing a shareholder to participate in an additional proxy solicitation should promote disclosure. "[I]n a democratic society, rival groups must stand in a fairly equal position in regard to their opportunities to place issues and candidates before the voters." E. ARANOW & H. EINHORN, *supra* note 3, at 9.

316. Many commentators who addressed this issue felt that such a scenario restricts the flow of information to shareholders instead of encouraging it. *Summary of Comments*, *supra* note 19, at 37.

317. The Commission cited duplicative costs as the primary reason in adopting the restriction on participating in an additional proxy solicitation. SEC DOCKET, *supra* note 13, at 503.

shareholders additional and unnecessary costs of printing and mailing lengthier proxy materials.³¹⁸ More significantly, exclusion of shareholder proposals concerning the same subject matter as other proxy solicitations for the same annual meeting does not hinder disclosure or prevent an informed shareholder vote.³¹⁹ This method would insure fairer representation and adequate disclosure while preventing duplicative costs and the arbitrary exclusion of shareholder proposals.

To facilitate a more equal representation within the proxy statement, a 1000-word limit should be placed on management's replies to a shareholder's proposal.³²⁰ This would provide a more equal forum for competing views.³²¹ Much of the present reason for shareholder participation in more than one proxy solicitation is to undermine management's ability to overwhelm an individual shareholder's proposal with lengthy replies.³²² While corporate proxy materials should give adequate coverage to each competing view, in reality, this rarely happens because management faces no limitations when responding to shareholder proposals.³²³ A 1000-word limit would help equalize management and shareholder influence on voters.

The 1000-word limitation does not, however, limit management's ability to inform shareholders of its own views as well as the ramifications of each shareholder proposal. Further, a 1000-word limitation would substantially improve readability of the proxy statements;³²⁴ and given the competent legal counsel retained by many large companies,

318. *Id.*

319. Arguably, since the subject matter is being brought before the shareholders in the proxy solicitation, the disclosure requirements have been met.

320. Presently, an issuer is under no word limitations when responding to shareholder proposals. Frequently, this leads to a situation where management simply overwhelms a shareholder proposal with its views.

321. *See supra* note 315.

322. *Summary of Comments, supra* note 19, at 37.

[W]ith regard to intracorporate communication, the corporate structure is not dissimilar to a one party town where the newspaper, radio, and TV station are under singular control. Those in dissent, without the resources to establish their own media, will be unable to effectively express their ideas and will rarely witness these ideas being so expressed by others. The remainder of the populace is, thus, deprived of the opportunity to consider or act upon a viewpoint critical of those in power.

Schulman, *supra* note 17, at 42.

323. Note, *supra* note 42, at 1372-73.

324. Proxy readability is one of the three goals of the Proxy Review Program. *See supra* note 13 and accompanying text.

this word limitation should not prevent management from performing their disclosure function.

B. 14a-8(A)(2): Notice Requirements

The amendments adopted by the Commission to Rule 14a-8(A)(2) are a positive step in streamlining the existing proxy rules. The Commission deleted various requirements from this provision which previously served little purpose.³²⁵ For example, a shareholder proponent will no longer have to notify an issuer of his intention to appear personally at the meeting.³²⁶ Also, a shareholder proponent will now be able to appoint a representative to present his proposal at the shareholders' annual meeting.³²⁷ Finally, a shareholder proponent must disclose to the issuer at the time he submits his proposal, his name, address, the number of shares he owns, and the dates upon which he acquired such securities.³²⁸

The previous requirement that a shareholder notify the issuer of his intention to appear personally at the annual meeting served little purpose; it did little to insure that a proposal would get presented at the annual meeting. In the past, shareholder proponents who had previously notified the issuer of their intention to appear frequently failed to present their proposals at the annual meeting.³²⁹ Moreover, there are sanctions available under Rule 14a-8(A)(2) to ensure that a proposal will be presented at the annual meeting.³³⁰ Under Rule 14a-8(A)(2) if a proponent fails to present a proposal at the annual meeting without good cause, the issuer is not required to include any proposals submitted by this proponent for the next two calendar years.³³¹ Consequently, the previous requirement was nothing more than a mere formality and its deletion is consistent with the goals of the Proxy Review Program.³³²

In conjunction with the deletion of the notice requirement, a shareholder proponent will now be able to appoint a representative to present his proposal at the annual meeting under Rule 14a-8(A)(2).³³³

325. Release No. 34-20091, *supra* note 24, at 2.

326. *Id.* See *supra* notes 161-63 and accompanying text.

327. 17 C.F.R. § 240.14a-8(A)(2) (1984). Reprinted in appendix. See *supra* notes 164-67 and accompanying text.

328. 17 C.F.R. § 240.14a-8(A)(2) (1984). Reprinted in appendix. See *supra* notes 168-72 and accompanying text.

329. *Summary of Comments*, *supra* note 19, at 38.

330. 17 C.F.R. § 240.14a-8(A)(2) (1984). Reprinted in appendix.

331. *Id.*

332. *Summary of Comments*, *supra* note 19, at 38.

333. See *supra* notes 164-67 and accompanying text.

Under this revision, it is more likely that a proposal will be presented at the annual meeting by an informed person.³³⁴ If a shareholder proponent is unable to present his proposal he should be able to choose a representative³³⁵ he feels is competent to present his proposal. Such a revision acknowledges that the proxy system's goals are competent presentation of proposals, and informed shareholder votes.³³⁶ Permitting shareholder proponents to choose a representative should allow them greater flexibility in the future. As a result, the Commission will no longer recognize a shareholder's attendance at a different shareholder meeting as a good cause for failure to present his proposal at the annual meeting.³³⁷ This decision is sound in light of the increased flexibility allowed a shareholder in presenting his proposal.³³⁸

However, the Commission's decision to eliminate the requirement that an issuer include the shareholder proponent's name, address, and number of shares owned in its proxy statement will inhibit comprehensive disclosure. Due to space limitations placed on a shareholder's proposal and its supporting statement, shareholders frequently need more information to properly assess the proposal;³³⁹ requiring that this information be included in the issuer's proxy materials may encourage shareholders to seek out additional information to formulate an informed vote.³⁴⁰ To require inclusion of a shareholder proponent's name, address, and number of shares in the proxy statement would properly encourage such inquiries.

C. 14a-8(A)(3) and 14a-8(D): Timeliness Requirements

Rules 14a-8(A)(3) and 14a-8(D) were amended to give issuers and the Commission more time to adequately assess a proposal.³⁴¹ Under Rule 14a-8(A)(3), a shareholder proponent will now have to submit a

334. SEC DOCKET, *supra* note 13, at 504. *See supra* note 165.

335. The representative must be chosen at the onset, and must be permitted under applicable state law to present the proposal for action at the meeting. SEC DOCKET, *supra* note 13, at 504.

336. SEC DOCKET, *supra* note 13, at 504.

337. Release No. 34-20091, *supra* note 24, at 2. *See supra* notes 175-76 and accompanying text.

338. *See supra* notes 164-67 and accompanying text.

339. *Summary of Comments*, *supra* note 19, at 57.

340. "The value of information is proportional directly to the extent it is utilized. Rule 14a-8 proceeds on this theory and seeks to stimulate participation in corporate affairs by affording security holders methods of contacting their fellows." Emerson & Latham, *SEC Proxy Regulation: Steps Towards More Effective Stockholder Participation*, 59 YALE L.J. 635 (1950).

341. *See supra* notes 178-82, 199-203 and accompanying text.

proposal thirty days earlier to allow the issuer more time to assess the merits of the proposal. Rule 14a-8(D) now requires the issuer to submit its intention to exclude a shareholder proposal ten days earlier, to give the Commission more time to assess both the proposal and the issuer's reason for excluding it.³⁴² Allowing both the issuer and the Commission more time to assess shareholder proposals should increase the effectiveness of the shareholder proposal process.

The new time periods for submission of proposals to the issuer and notification to the Commission of the issuer's intention to omit a proposal will better serve the interests of the parties involved.³⁴³ The issuers, frequently, were not able to adequately assess the shareholder proposals they received. The inadequacies of the previous time constraints did a great disservice to shareholder proponents.³⁴⁴ Under the new revision, issuers will be better able to assess the merits of a shareholder proposal.³⁴⁵ Also, with more time to examine shareholder proposals, the issuers will be less likely to make frivolous requests for no-action letters from the staff. Finally, the additional time the Commission has to examine shareholder proposals will allow for a more consistent interpretation of the shareholder proposal rule.

However, increasing the time allowed to the issuer may have a very undesirable effect when considered in conjunction with the revised holding period requirement.³⁴⁶ The 120 day advance submission period for the shareholder proponent, when combined with the one year holding period requirement, means that a shareholder must wait sixteen months before he can submit a shareholder proposal for inclusion in the issuer's proxy materials.³⁴⁷ This will substantially increase the inequities for recent shareholders.³⁴⁸ This prolonged submission period will apply without consideration of the merits of the proposal.³⁴⁹

342. SEC DOCKET, *supra* note 13, at 504. The Commission believes such a change will provide the staff with more time to deal with the increased number and complexity of the security holder proposals being submitted. *Id.* at 512.

343. *Id.* at 504.

344. *Id.* Also, the desire for expediency and simplicity in the performance of its administrative duties has put pressure on the staff to cut corners where possible. Note, *The SEC and No-Action Decisions Under Proxy Rule 14a-8: The Case For Direct Judicial Review*, 84 HARV. L. REV. 847 (1971).

345. SEC DOCKET, *supra* note 13, at 504.

346. *Summary of Comments*, *supra* note 19, at 45.

347. *Id.*

348. In addition to the burden of the new eligibility requirements adopted in Rule 14a-8(A)(1).

349. See *supra* note 304 and accompanying text.

This undesirable effect would be eliminated if the minimum investment and holding period requirement were replaced by the shareholder submission fee. Under this arrangement, increasing the time periods the staff and issuers have to deal with shareholder proposals would no longer result in inequities for recent shareholders. A useful deterrent for frivolous shareholder proposals would still exist³⁵⁰ but without the arbitrary exclusion of valid shareholder proposals that will occur under the recently-revised eligibility requirements. The use of the shareholder submission fee would not require more drastic measures to eliminate the perceived abuses of the shareholder proposal rule.

D. 14a-8(A)(4): Number of Proposals

In Rule 14a-8(A)(4), the Commission has reduced the number of proposals a shareholder can submit from two to one.³⁵¹ This reduction is both unjustified and unnecessary. Moreover, this will seriously hinder a shareholder's ability to bring important issues before the other shareholders.³⁵²

The reduction of the number of proposals a shareholder can submit will unreasonably restrict shareholder access to the corporate proxy machinery. While the purported goal of this revision is to prevent abuse of the shareholder proposal process, the Commission has failed to show that limiting the number of proposals will further this goal.³⁵³ Given the other revisions to Rule 14a-8, this reduction may be unnecessary to prevent shareholder abuse.³⁵⁴ Instead, it will result in the suppression of competing ideas. Also, given the scope and complexity of corporate activity, a shareholder may have more than one valid area of concern;³⁵⁵ the shareholder now will be unable to bring these additional issues before the shareholder body.

A fee requirement would eliminate the need to reduce the number of proposals a shareholder can submit under Rule 14a-8(A)(4). The imposition of a fee on shareholder proponents, if added to the previous requirement of two proposals per proponent,³⁵⁶ would

350. Shareholder proponents who submit frivolous proposals will forfeit their shareholder submission fee.

351. Release No. 34-20091, *supra* note 24, at 3.

352. Many of the commentators responding to this issue argued that, "the need to implement the reduction had not been demonstrated, that there is not convincing evidence of abuse or excessive burdens in connection with the previous rule." *Summary of Comments*, *supra* note 19, at 49-50.

353. *Id.*

354. *Id.*

355. *Id.*

356. 17 C.F.R. § 240.14a-8(A)(4) (1983).

adequately control the number of proposals submitted. A fee requirement, consequently, would allow shareholder proponents to adequately address relevant issues without significantly restricting shareholder access to the corporate proxy machinery.

E. 14a-8(B)(1): Supporting Statements

The revisions to Rule 14a-8(B)(1) will allow shareholder proponents greater flexibility when drafting a proposal and supporting statement. A shareholder proponent is now able to allocate the 500-word limit between his proposal and supporting statement any way he chooses.³⁵⁷ Significantly, this revision will not increase the burden of disclosure on the issuer,³⁵⁸ instead, it alleviates the arbitrary division of a shareholder's proposal and supporting statement, thereby improving proxy readability.³⁵⁹ This will allow for a "more lucid and cogent presentation of a proposal."³⁶⁰

Under these circumstances, the advantages of the revisions to Rule 14a-8(B)(1) extend beyond those that accrue to the individual shareholder proponent; these revisions will greatly enhance proxy readability for fellow shareholders.³⁶¹ Issuers are now required to include supporting statements in the proxy materials even when they do not oppose the proposal.³⁶² Hence, the shareholder proposal and supporting statement will have greater clarity and be more complete. Requiring inclusion of supporting statements, even though the issuer does not oppose the shareholder proposal, should help promote a more informed shareholder vote.³⁶³ Fairness requires that shareholders be given proxy materials with complete and cogent proposals to adequately assess such proposals before casting their vote.³⁶⁴

357. Release No. 34-20091, *supra* note 24, at 3. See *supra* note 191 and accompanying text.

358. *Summary of Comments*, *supra* note 19, at 46. See also SEC DOCKET, *supra* note 13, at 505.

359. Release No. 34-20091, *supra* note 24, at 3.

360. *Summary of Comments*, *supra* note 19, at 46. See also, Securities Exchange Act of 1934 Release No. 34-17517 (Feb. 5, 1981), 46 Fed. Reg. 12,011 (1981). 21 SEC DOCKET (CCH) 1546 (1981).

361. Release No. 34-20091, *supra* note 24, at 3.

362. *Id.*

363. "... anyone who solicits proxies, whether management or an outside group, must supply the security holder with adequate information so that he may exercise an informed judgment in voting his shares." Emerson & Latham, *The SEC Proxy Proposal Rule: The Corporate Gadsby*, 19 U. CHI. L. REV. 807 (1952). See *supra* note 193.

364. See *supra* note 192.

F. 14a-8(B)(2): Identification of Proponent

The revision to Rule 14a-8(B)(2) will require issuers, instead of the Commission, to provide names and addresses of shareholder proponents *upon request*.³⁶⁵ This is a positive revision which will eliminate the present administrative problems such requests commonly cause³⁶⁶ and should be required of the issuer and not the Commission. Since shareholder proponents must now submit their names and addresses along with their proposals³⁶⁷ the issuer will have this information at its disposal. To further improve this positive revision, the issuer should be *required* to include the shareholder proponent's name and address in the proxy materials to encourage communication among the shareholders.

G. 14a-8(C)(1): Proper Subject for Shareholder Action

The revision of the note accompanying Rule 14a-8(C)(1) to reflect that state law governs the admissibility of a proposal creates a meaningless distinction. The revision makes it clear that state law and not the staff's practice governs whether a proposal, submitted in the form of a recommendation, is includable in an issuer's proxy materials.³⁶⁸ However, most state corporation laws offer little guidance because they are drafted in vague terms.³⁶⁹ Also, if many of the "management statutes"³⁷⁰ were interpreted narrowly by the staff, the shareholder proposal process would become a nullity. As a result, the staff's practice of allowing the inclusion of a proposal which takes the form of a recommendation is necessary to preserve "fair corporate suffrage."

The inherent difficulty in applying the "proper subject" test³⁷¹ stems from the fact that most state corporation statutes employ sweeping language.³⁷² Specifically, in most states the board of directors is granted the general power to manage the business and affairs of the

365. "The staff has not been able in all cases to respond in a timely fashion to security holder's requests for the name and address of any particular proponent." SEC DOCKET, *supra* note 13, at 506.

366. See *supra* note 194.

367. 17 C.F.R. § 240.14a-8(A)(2) (1984). Reprinted in appendix.

368. Release No. 34-20091, *supra* note 24, at 3.

369. L. LOSS, 2 SECURITIES REGULATION 905 (2d Ed. 1961). See also *supra* note 49 and accompanying text.

370. Usually these statutes contain provisions which expressly require that certain types of corporate action be initiated by the board of directors.

371. Determining whether a proposal submitted by a shareholder concerns a proper subject for shareholder action under applicable state law.

372. Black & Sparks, *supra* note 114, at 966.

company.³⁷³ Complicating this analysis is the lack of case law interpreting such statutes. As a result, the only way the staff can effectuate the purpose of Rule 14a-8(C)(1) is to adopt a federal "common law" under the guise of interpreting state law.³⁷⁴ Within this "common law," there is some authority which supports a shareholder's right to make recommendations to management.³⁷⁵

Where proposals are submitted in the form of a recommendation, the pertinent inquiry should concern the form rather than the substance of the proposal. The Commission interprets the corporate law of most states as permitting shareholder proposals in the form of recommendations.³⁷⁶ Thus, it is the staff's practice to require inclusion of a proposal submitted in the form of a recommendation despite the fact that a shareholder has no power to direct this type of action.³⁷⁷ Through this practice, the Commission generally seeks to promote shareholder participation. Requiring inclusion of advisory proposals in the issuer's proxy materials is a positive solution to possible conflicts with state laws.³⁷⁸ Given the present trend³⁷⁹ and composition of many of the state corporation laws,³⁸⁰ the Commission has chosen "the lesser of two evils."³⁸¹

The new language adopted by the Commission in the note accompanying Rule 14a-8(C)(1) will not alter the staff's present practice of elevating form over substance.³⁸² The staff will still resort to the same practice as before due to the vague language of the state

373. Schwartz, *supra* note 33, at 440.

374. Elliot, *supra* note 27, at 54. See also Schwartz, *supra* note 33, at 440.

375. Release No. 34-20091, *supra* note 24, at 3.

376. See *supra* note 213 and accompanying text.

377. Kapp & Bancroft, *No-Action Highlights*, 3 SEC. REG. L.J. 71, 73-80 (1975). It is important to note that a shareholder proposal submitted in the form of a recommendation, even if adopted by the stockholders, would not be binding on the board of directors.

378. Note, *supra* note 42, at 1347.

379. Professor Cary characterizes the recent trend as a "race for the bottom," with Delaware leading the way. Other states simply want to encourage companies to stay at home and these states therefore try to emulate Delaware by revising their acts along similar lines. Today, state corporation laws are "described as 'enabling' acts — enabling management to operate with minimal interference." Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L.J. 663, 666 (1974). See also Fischel, *The "Race To The Bottom" Revisited: Reflections on Recent Developments in Delaware's Corporation Laws*, 76 NW. U.L. REV. 913 (1982).

380. See *supra* note 49.

381. If the "management" statutes are interpreted too narrowly, Rule 14a-8 would become a nullity. In a practical sense, the staff's elevation of form over substance gives some meaning to the shareholder proposal process.

382. *Summary of Comments*, *supra* note 19, at 83.

corporation statutes.³⁸³ Given that state law is often of little help in determining whether a proposal can be excluded, it appears that the staff has little choice but to elevate form over substance. If the staff strictly interprets the state "management statutes,"³⁸⁴ it will unreasonably restrict shareholder access to the issuer's proxy materials. However, the staff's practice of including proposals submitted in the form of a recommendation under Rule 14a-8(C)(1) is the only instance when it is advisable to elevate form over substance in interpreting Rule 14a-8.³⁸⁵

H. 14a-8(C)(4): Personal Claim or Grievance

The "personal grievance" exclusion permits management to exclude proposals which primarily address the individual shareholder proponent's dissatisfaction instead of a broad managerial concern.³⁸⁶ The new revision has both subjective and vague terms³⁸⁷ that will be likely to cause the staff greater interpretive problems with the "personal grievance" exclusion. Since all shareholder proposals are motivated by some type of dissatisfaction,³⁸⁸ a more subjective analysis could result in unreasonably restricting shareholder access to the issuer's proxy machinery.

The revision adopted by the Commission in Rule 14a-8(C)(4) will only create additional interpretive problems for the staff. Rule 14a-8(C)(4) will now require the staff to determine whether a proposal is designed to result in a benefit not shared by other shareholders.³⁸⁹ This new language is even more susceptible to a broad interpretation by the staff than was the previous language.³⁹⁰ Further, given the

383. See *supra* note 49 and accompanying text.

384. See *supra* note 370. Essentially these corporation statutes do not address stockholder action.

385. See *infra* notes 418-19 and accompanying text.

386. Release No. 34-20091, *supra* note 24, at 4.

387. *Summary of Comments*, *supra* note 19, at 60. Also, there is a greater danger that they will be interpreted by the staff more broadly than was the case with the previous provision. *Id.*

388. STAFF REPORT, *supra* note 80, at 184.

389. Release No. 34-20091, *supra* note 24, at 4. A proposal could conceivably be excluded from an issuer's proxy material, even though it might relate to matters which may be of general interest to all security holders, if it is clear from the facts presented by the issuer that the proponent is using the proposal as a tactic designed to redress a personal grievance or further a personal interest. SEC DOCKET, *supra* note 13, at 507.

390. *Summary of Comments*, *supra* note 19, at 60. In referring to the previous language of Rule 14a-8(C)(4), the Commission noted that this was, "the most subjective provision and definitely the most difficult for the staff to administer . . ." SEC DOCKET, *supra* note 13, at 507.

diversity of shareholder interests, almost any proposal can be perceived as not designed to result in a benefit to the shareholders as a whole.³⁹¹

To require the staff to go beyond the face of the proposal to determine personal motivation is inappropriate.³⁹² The Commission believes that sophisticated shareholder proponents have abused Rule 14a-8(C)(4) in the past by drafting their proposals in sufficiently broad terms to obscure the personal interests that motivated their proposals.³⁹³ The result is that an individual's interests are only discernible in varying degrees. Notwithstanding, the staff is unequipped with any effective fact-finding mechanisms to properly discern a shareholder proponent's state of mind.³⁹⁴ Hence, to ask the staff to make a subjective determination given these circumstances will only result in inconsistent interpretation of Rule 14a-8(C)(4).³⁹⁵

If Rule 14a-8(C)(4) is interpreted broadly it could be used by issuers to unreasonably restrict shareholder access to the issuer's proxy materials. Moreover, management's attempt to exclude a proposal under Rule 14a-8(C)(4) may primarily reflect their opposition to the shareholder's proposal, which proposal, if later included in the proxy statements would force management to publicly defend its position in the proxy materials. Also, issuers are just as likely as shareholders, if not more so, to fully exploit broadly-interpreted provisions of Rule 14a-8.³⁹⁶

I. 14a-8(C)(5): Not Significantly Related to the Issuer's Business

The new objective economic standard³⁹⁷ adopted by the Commission to Rule 14a-8(C)(5), requiring that a shareholder's proposal relate to at least five percent of the issuer's business, ignores the practical realities of its application.³⁹⁸ This standard effectively insulates the

391. *Summary of Comments*, *supra* note 19, at 61.

392. *See supra* notes 72, 84 for some problems likely to be encountered.

393. Release No. 34-20091, *supra* note 24, at 4.

394. Schwartz, *supra* note 33, at 446. Essentially the staff is furnished only with documents and an opinion of counsel to make a decision whether the proposal must be included in the proxy statement. "The only thing it can rationally decide is whether the language of the proposal is proper for shareholders: motive, on the evidence before the Commission, is entirely speculative." *Id.*

395. *Summary of Comments*, *supra* note 19, at 60.

396. *Id.*

397. Karmel, *supra* note 14, at 9.

398. 17 C.F.R. § 240.14a-8(C)(4) (1984). *Reprinted in* appendix.

largest companies from shareholder proposals on important issues.³⁹⁹ Issuers will be likely to perceive the economic criteria as overshadowing the rest of the provision in Rule 14a-8(C)(5).⁴⁰⁰ Equally important, a broad interpretation of Rule 14a-8(C)(5) by the staff will directly contradict the Supreme Court's holding in *Bellotti*.⁴⁰¹ A more appropriate economic test would be the application of a stated percentage on a sliding scale to take into consideration the amount of business an issuer transacts. In addition, a liberal interpretation of the provision that permits inclusion of economically insignificant proposals, will insure that Rule 14a-8(C)(5) is not overshadowed by the economic criteria.

A particularly disturbing trend in the amendments on the whole, is that in the search for more objective standards, the Commission has overlooked the practical realities of many corporate undertakings.⁴⁰² Given the large size of many corporations, matters of substantial concern to shareholders are quite likely to involve less than a stated percentage of the issuer's business.⁴⁰³ The revision of the Rule 14a-8(C)(5) requiring that a shareholder proposal relate to at least five percent of the company's business, ignores this problem. Taken to a logical extreme, the larger and more diversified the company is, the less likely it is that shareholders will be able to submit proposals on matters of corporate policy.⁴⁰⁴ Thus, those corporations with the largest impact on society will be less accountable to their shareholder constituency than smaller, more concentrated corporations.⁴⁰⁵ Focusing on economic criterion conceivably silences shareholder input on important political and ethical implications of company activities despite these vital areas' economic insignificance under the new revision to Rule 14a-8(C)(5).

399. STAFF REPORT, *supra* note 80, at 192. Such a result would seem to be diametrically opposed to the underlying purpose of Section 14 of the 1934 Securities Exchange Act. *Id.* See *supra* note 34.

400. *Summary of Comments*, *supra* note 19, at 65.

401. *Id.* See *supra* notes 118-20 and accompanying text.

402. This is also readily apparent in the revisions to Rule 14a-8(C)(12) adopted by the Commission. See *infra* notes 435-37 and accompanying text.

403. Schwartz & Weiss, *supra* note 5, at 667. Also, in light of the recent trend of public corporations becoming increasingly politicized, areas which may now be economically insignificant under Rule 14a-8(C)(5) may be of substantial concern to shareholders. Karmel, *supra* note 14, at 12.

404. *Summary of Comments*, *supra* note 19, at 65. Further complicating this is the fact that many social and ethical issues cannot be easily translated into a percentage of assets or revenue. *Id.* at 64.

405. STAFF REPORT, *supra* note 80, at 191. Thus, in those companies with the largest revenues or asset values shareholders may be unable to submit proposals addressing timely and important issues when shareholders in a smaller company are allowed to.

Issuers may place greater weight on the economic significance test of Rule 14a-8(C)(5) than on the remainder of the provision. The remaining provision provides that if a proposal is significantly related to the issuer, although economically insignificant, it may not be excluded from the issuer's proxy materials.⁴⁰⁶ However, a potential problem with the revision to this rule is that many issuers may automatically request a no-action letter for any proposal that is deemed economically insignificant. This will only further escalate the costs of compliance with the shareholder proposal rule for issuers and unnecessarily burden the Commission's staff.

Beyond this, Rule 14a-8(C)(5), if interpreted broadly by the staff, will be inconsistent with recent Supreme Court precedent. In *Bellotti*, the Supreme Court held that shareholders could decide, "through the procedure of corporate democracy, whether their corporation should engage in debate on public issues."⁴⁰⁷ The *Bellotti* case, in conjunction with the increasing visibility of corporate political activity,⁴⁰⁸ should make it more difficult for an issuer to successfully exclude a proposal that does not have a significant relationship to the issuer's business.⁴⁰⁹ Instead, the revision of Rule 14a-8(C)(5) seems to disregard *Bellotti* to the extent that the staff applies the "significantly related" exclusion broadly.⁴¹⁰

Exclusion of shareholder proposals that do not relate to five percent of the issuer's business pursuant to Rule 14a-8(C)(5) ignores the practical realities of the size of many corporations.⁴¹¹ A more appropriate approach is to apply a stated percentage, for instance one percent,⁴¹² on a sliding scale. In companies with relatively small earnings, a proposal would have to affect at least one percent of the

406. SEC DOCKET, *supra* note 13, at 509. "For example, the proponent could provide information that indicates that while a particular corporate policy which involves an arguably insignificant portion of an issuer's business, the policy may have a significant impact on other segments of the issuers business or subject the issuer to significant contingent liabilities." *Id.*

407. 435 U.S. at 795. See *supra* notes 116, 118-20 and accompanying text.

408. See *supra* note 403.

409. Propp, *supra* note 18, at 112.

410. See *supra* note 120 and accompanying text.

411.

For example, Neuhauser noted that 5% of Exxon's 1981 revenues amounted to \$5,750,000,000, which was more revenue than all but 59 of the Fortune 500 companies. He observed that if such companies as Gulf & Western, Deere, Honeywell or Alcoa were subsidiaries of Exxon in 1981, they would not be significant subsidiaries for purposes of Rule 14a-8.

Summary of Comments, *supra* note 19, at 65.

412. This figure was used before 1976 and was later removed in the 1976 amend-

issuer's business in order to be included in the proxy statement. However, in companies with extremely large earnings, a proposal would only have to affect a markedly lower percentage of business like one-tenth of a percent. This sliding scale economic test would consider the extent of operations of larger companies and adjust the percentage test accordingly. In this respect, those companies which have the largest revenues would not be insulated from shareholder proposals on important social and political issues relating to their business.

Shareholder proposals that have great significance which transcends their economic importance will not always be excluded under Rule 14a-8(C)(5).⁴¹³ This clause in the revised provision should theoretically serve as an adequate check on the issuers so that the economic criterion does not overshadow the rest of the provision. Many aspects of a proposal that fails to satisfy the economic test may be sufficiently important to shareholders that their exclusion will impede adequate disclosure. Therefore, it is imperative that the staff administer Rule 14a-8(C)(5) in such a way that the economic criterion does not overshadow the rest of the exclusion.

J. 14a-8(C)(7): Ordinary Business

The interpretive change to Rule 14a-8(C)(7) adopted by the Commission is a positive attempt to eliminate the staff's previous practice which elevated form over substance.⁴¹⁴ No longer must a shareholder proposal be included in the issuer's proxy material solely because it requests that a report be compiled for the shareholders.⁴¹⁵ Under the present revision the staff will first look to the issues the report addresses;⁴¹⁶ if the report concerns only ordinary business, it will be excluded from the issuer's proxy materials.⁴¹⁷

To eliminate the staff's practice of elevating form over substance in administering Rule 14a-8(C)(7), the Commission has adopted an appropriate interpretive change.⁴¹⁸ In the past, the staff's practice was

ments to Rule 14a-8. See *supra* note 228 and accompanying text.

413. 17 C.F.R. § 240.14a-8(C)(5) (1984). Reprinted in appendix.

414. Release No. 34-20091, *supra* note 24, at 3.

415. *Id.* Previously, the staff's position was based on the premise that issuers do not prepare and issue reports on specific matters to shareholders or form committees to study particular aspects of its business as part of their ordinary business operations. SEC DOCKET, *supra* note 13, at 510.

416. Release No. 34-20091, *supra* note 24, at 4.

417. *Id.*

418. *Summary of Comments*, *supra* note 19, at 67. Among the commentators responding to this issue there was near unanimous concurrence with the new interpretive position. *Id.*

to include all proposals that requested a report to the shareholders on some matter, without regard to the substantive issues addressed in the report. This practice imposed additional costs on both shareholders and issuers when the proposal addressed an issue solely within the province of management.⁴¹⁹ The staff believes that many issuers do not compile such reports as a matter of ordinary business.⁴²⁰ However, this belief should never be the sole reason for requiring inclusion of a shareholder's proposal. Instead, the staff should evaluate a proposal on its merits without regard to the seemingly arbitrary objective standards which have developed.⁴²¹

The staff's previous practice was to interpret the "ordinary business" exclusion without considering the subject matter of the proposal. Frequently shareholders would address issues entirely within the province of management and add a request for a report in order to avoid the exclusionary impact of Rule 14a-8(C)(7).⁴²² In this way the shareholder proponent could effectively circumvent the "ordinary business" exclusion. If an issuer sufficiently proves that such a report is a matter of ordinary business, then the staff should not burden the issuer and its shareholders with the costs of including such a proposal in the proxy materials. Therefore, a request for a report should not be outcome determinative, but rather should be only one factor for the staff to examine in deciding whether a proposal is excludable.

The staff must, ultimately, look to statutory and decisional law of the issuer's domicile to determine whether a proposal should be excluded.⁴²³ Still, the staff must realize that some proposals which require a management decision may not be excludable under Rule 14a-8(C)(7); some requests for reports are anything but ordinary business, and may concern activities that shareholders may regard as important.⁴²⁴ Equally important, very real benefits as well as improved disclosure can result from having an issuer justify its present practices in a report.⁴²⁵

419. *Id.*

420. *Id.* See *supra* note 415.

421. Black & Sparks, *supra* note 114, at 977. This would require the staff to consider in each instance whether the type of information sought by the shareholder proponent involved is a matter in which the shareholders, as opposed to the board of directors, have a legitimate decision-making interest. *Id.*

422. SEC DOCKET, *supra* note 13, at 510.

423. However, state law precedent is rarely conclusive as to what is or is not ordinary business. SEC DOCKET, *supra* note 13, at 510.

424. Eisenberg, *supra* note 212, at 915.

425. *Summary of Comments*, *supra* note 19, at 67.

K. 14a-8(C)(10): Mootness

To insure adequate disclosure to its shareholders, issuers should be required to include shareholder proposals unless they are already fully implemented. The present "mootness" standards⁴²⁶ adopted by the Commission are imprecise and subjective.⁴²⁷ Information regarding the speed and extent of management's compliance with shareholder suggestions is a valid shareholder concern.⁴²⁸ To allow an issuer to exclude shareholder proposals which are "substantially" complied with leaves shareholders uninformed of many important corporate concerns.

The Commission has adopted a significant interpretive change to Rule 14a-8(C)(10) in determining whether a proposal can be excluded for mootness. However, the mootness provision's vague and subjective language⁴²⁹ will cause many interpretive problems for the staff; it simply lacks any objective guidelines for determining if a proposal is "substantially implemented." While the language itself may not be overinclusive, there is a danger that the staff's interpretation may be. The result is that Rule 14a-8(C)(10), if interpreted broadly, will unreasonably restrict corporate disclosure.

Issuers should not be allowed to partially implement a shareholder's proposal in order to avoid including it in their proxy materials. Specifically, the part of the proposal not implemented is often the most crucial to the shareholders.⁴³⁰ The present revision permits the issuer to avoid confronting the shareholder's proposal by just such a partial implementation of his proposal. In order to adequately serve the disclosure function, the issuer should allow the shareholders to be able to assess and vote on every proposal that is proper for their consideration.

Under Rule 14a-8(C)(10) the standards for determining whether a shareholder proposal can be excluded are too subjective for effective staff implementation. The shareholders will become an uninformed constituency if this provision is interpreted broadly by the staff. Management will be able to avoid undesired debate and disclosure by partial implementation. An issuer should have to justify why a

426. See *supra* note 248 and accompanying text.

427. *Summary of Comments, supra* note 19, at 67. Several commentators believe the new interpretive standard would create greater interpretive difficulties and unreasonably constrain disclosure to shareholders. *Id.*

428. *Id.*

429. Rule 14a-8(C)(10) now permits the omission of proposals that are "substantially implemented by the issuer."

430. *Summary of Comments, supra* note 19, at 72.

certain aspect of a proposal has not been fully implemented and how it intends to rectify this in the future; such information may be necessary for a shareholder to evaluate the performance of current management. Therefore, the issuers should be required to include proposals regardless of their partial implementation and then indicate in their management's statement which parts of the proposals are already implemented.

L. 14a-8(C)(12): Repeat Proposals

The revisions to Rule 14a-8(C)(12) are both oppressive and unjustified. The previous rule excluded proposals that were *substantially the same* as proposals submitted in previous years.⁴³¹ In contrast, under the new revision, proposals that relate to *substantially the same subject matter* as proposals submitted in prior years are excludable.⁴³² In addition, the minimum percentage tests for resubmission of proposals in subsequent years are increased.⁴³³ Collectively, these revisions only serve to further alienate shareholders and emasculate the shareholder proposal process.⁴³⁴

The provision of Rule 14a-8(C)(12) allowing proposals that are "substantially the same subject matter" as proposals included in prior years to be excluded, will create a host of interpretive problems. The wording of a proposal is of considerable importance to shareholders, particularly institutional investors.⁴³⁵ Therefore, because the votes of these shareholders may turn on slight changes in the language of the resolution, the Commission's determination not to allow shareholders a full opportunity to modify their approach to any given subject is unsound. If the overall thrust of a proposal changes from one year to another, particularly when the modifications are responsive to management's arguments concerning the shortcomings of the proposed action, the staff should refrain from treating the modified proposal as a repeat proposal. The revisions to Rule 14a-8(C)(12) are likely to unduly burden the reasonable exercise of "fair corporate suffrage" which Congress intended section 14(a) of the 1934 Act to promote.⁴³⁶

Loosely interpreted, this exclusion would mean that concerned shareholders could raise subject matters as broad as nuclear power

431. 17 C.F.R. § 240.14a-8(C)(12) (1983).

432. 17 C.F.R. § 240.14a-8(C)(12) (1984). *Reprinted in* appendix.

433. *See supra* notes 256-60 and accompanying text.

434. *Summary of Comments, supra* note 19, at 79.

435. Schwartz & Weiss, *supra* note 5, at 679.

436. *Id.* at 683. *See supra* notes 12, 39.

or South Africa only once every five years.⁴³⁷ Therefore, the staff should interpret Rule 14a-8(C)(12) in light of the goals of the shareholder proposal process and the social context in which companies operate. Insensitive enforcement by the staff of Rule 14a-8(C)(12) could reduce much of the present effectiveness of the shareholder proposal process.

Rule 14a-8(C)(12) fails to acknowledge that shareholder votes may turn on the language of the proposal.⁴³⁸ Essentially, the present revisions to Rule 14a-8(C)(12) present shareholders with an all-or-nothing dilemma. If a shareholder votes against a proposal he must realize that he has also effectively voted against more favorable solutions to the same issue; such an outcome does not benefit shareholders and is inconsistent with the notion of "fair corporate suffrage."

In conjunction with the revision of the "substantially the same" language, the Commission has further restricted "fair corporate suffrage" by increasing the percentage tests for resubmission of proposals in subsequent years.⁴³⁹ If a proposal is initially included in the issuer's proxy material, it must gain a stated percentage of the votes for inclusion in the proxy materials in subsequent years.⁴⁴⁰ However, the importance of the shareholder proposal process exceeds mere tabulation of a numerical vote. At the outset, it is extremely doubtful whether progress may be defined mathematically. Quite simply, "[t]he subject matter of the proposal process is competing ideas and popularity affords no useful or enduring denominators of a proposal's relative

437. Lydenberg, *supra* note 16, at 65.

438. The BA Investment Management Corp., a subsidiary of BankAmerica Corp., recently made the following comment to the Commission:

On many occasions we have considered proposals in which we agree with the general purpose but disagree with the specifics. If other shareholders reject a proposal for such a reason, the proponent may wish to reformulate the proposal so as to make it more passable. The improved version of the proposal may then be resubmitted to the shareholders the following year and may very well receive more support. We feel that this is a constructive process, one in which the most desirable form of proposal may be developed and eventually passed by the shareholders.

Letter from Thomas H. Andrews, Senior Vice President, & Daphne M. O'Keefe, Corporate Social Responsibility Analyst, BA Investment Management Corp., to George A. Fitzsimmons, Secretary, SEC, dated Sept. 5, 1976 (File No. S7-643).

439. See *supra* note 256 and accompanying text. The failure of shareholder proposals to carry or win larger votes is no criterion to judge the validity of a proposal. Emerson & Latham, *supra* note 361, at 835.

440. 17 C.F.R. § 240.14a-8(C)(12) (1984). *Reprinted in* appendix.

or ultimate worth."⁴⁴¹ In spite of these misgivings about the percentage tests for resubmission, the Commission has unnecessarily increased the stated percentage figures used in the test.⁴⁴²

Increasing the minimum percentage tests for resubmission for shareholder proposals is unjustified given the realities of shareholder voting. The small number of favorable votes most shareholder proposals receive is largely a function of management's recommendations in the proxy materials for or against a specific proposal.⁴⁴³ In addition, unmarked proxies⁴⁴⁴ are a large factor affecting the results of the shareholder vote. Management has discretion to vote these unmarked proxies against the various shareholder proposals. Increasing the minimum percentage tests for resubmission also favors the larger companies.⁴⁴⁵

Under the revisions of Rule 14a-8(C)(12) that increase the minimum percentage tests, larger companies with a substantial impact on society are insulated from being accountable to their shareholders. To prevent this problem, the minimum percentage tests should be applied on a sliding scale to fairly reflect those areas of relative importance. The revised minimum percentage tests fail to reveal substantial shareholder interest because they do not consider absolute numbers. The previous limits of three percent and six percent for the first and second years respectively should continue to apply.⁴⁴⁶ Ten percent should be the upper limit for any years thereafter. These figures, however, should be adjusted downward for companies with a large shareholder body.⁴⁴⁷

V. CONCLUSION

The proxy rules governed by the Commission are principally designed to assure proper disclosure. In furtherance of this goal, Rule 14a-8 permits direct participation by shareholders in the affairs of

441. Emerson & Latham, *supra* note 361, at 835.

442. *Summary of Comments*, *supra* note 19, at 78. It was argued that the abuses of the existing rule have been rare and do not justify the revision proposed, that any abuse can be dealt with under a stricter application of the present interpretation. *Id.*

443. STAFF REPORT, *supra* note 80, at 162.

444. These are proxies which are signed in blank and voted at management's discretion. Such proxies are a large factor affecting the results of voting on shareholder proposals.

445. STAFF REPORT, *supra* note 80, at 171.

446. See 17 C.F.R. § 240.14a-8(C)(12) (1983).

447. *Summary of Comments*, *supra* note 19, at 171. For instance, companies like Exxon with approximately 846 million investors should be treated differently than appreciably smaller companies for purposes of Rule 14a-8(C)(12).

every corporation whose proxy solicitation is subject to the Commission's proxy rules. In fact, there is probably no rule governed by the Commission which offers more opportunity for practical application to more individual shareholders.⁴⁴⁸ Throughout its forty-year history, Rule 14a-8 has been perceived as an exemplar of "fair corporate suffrage." Nevertheless, some changes are necessary to insure that Rule 14a-8 continues to function effectively.

The current revisions to Rule 14a-8 are the Commission's response to the perceived abuses by shareholders. Indeed, some of the revisions adopted by the Commission maintain "fair corporate suffrage" while achieving the goals of the Proxy Review Program. On the whole, however, the Commission has perceived the problem incorrectly in some instances and overacted in others. The Commission has fashioned numerous formulae permitting issuers to decide whether proposals may be omitted from corporate proxy materials without reaching the merits of the proposal. Active use of the corporate proxy machinery does not, by itself, constitute abuse.⁴⁴⁹ In addition, concerns about the cost of the shareholder proposal process are greatly exaggerated.

The present revisions will have little or no positive effect on the costs to issuers of compliance with Rule 14a-8. However, the present revisions will have a great negative impact on corporate disclosure and the notion of "fair corporate suffrage." In the past, the Commission has gone to great lengths to insure shareholder access to the corporate proxy machinery. Whether such a commitment on the Commission's part will persist in the future remains to be seen.

SÉAN PATRICK O'BRIEN

448. Black & Sparks, *supra* note 30, at 1-2.

The proxy rules are very likely the most effective disclosure device in the SEC scheme of things. The proxy literature, unlike application for registration and the statutory reports, gets into the hands of investors. Unlike the Securities Act prospectus, it gets there in time. It is more readable than any of these documents. And it gets to a good many people who never see a prospectus

Loss, *supra* note 370, at 1027.

449. Release No. 34-20091, *supra* note 24, at 7.

APPENDIX

Securities Exchange Act of 1934 Release No. 34-20091 (Oct. 3, 1983) 48 Fed. Reg. 38218 (1983).

Text of Revised Rule 14a-8: § 240.14a-8 Proposals of security holders.

(A) If any security holder of an issuer notifies the issuer of his intention to present a proposal for action at a forthcoming meeting of the issuer's security holders, the issuer shall set forth the proposal in its proxy statement and identify it in its form of proxy and provide means by which security holders can make the specification required by Rule 14a-4(B) [17 CFR § 240.14a-4(B)]. Notwithstanding the foregoing, the issuer shall not be required to include the proposal in its proxy statement or form of proxy unless the security holder (hereinafter, the "proponent") has complied with the requirements of this paragraph and paragraphs (B) and (C) of this section:

(1) *Eligibility.* (i) At the time he submits the proposal, the proponent shall be a record or beneficial owner of at least 1% or \$1000 in market value of securities entitled to be voted at the meeting and have held such securities for at least one year, and he shall continue to own such securities through the date on which the meeting is held. If the issuer requests documentary support for a proponent's claim that he is the beneficial owner of at least \$1000 in market value of such voting securities of the issuer or that he has been a beneficial owner of the securities for one or more years, the proponent shall furnish appropriate documentation within 14 calendar days after receiving the request. In the event the issuer includes the proponent's proposal in its proxy soliciting material for the meeting and the proponent fails to comply with the requirement that he continuously hold such securities through the meeting date, the issuer shall not be required to include any proposals submitted by the proponent in its proxy material for any meeting held in the following two calendar years.

(ii) Proponents who deliver written proxy materials to holders of more than 25 percent of a class of the issuer's outstanding securities entitled to vote with respect to the same meeting of security holders will be ineligible to use the provisions of Rule 14a-8 for the inclusion of a proposal in the issuer's proxy materials. In the event the issuer includes a proponent's proposal in its proxy material and the proponent thereafter delivers written proxy materials to the holders of more than 25 percent of a class of the issuer's outstanding securities entitled to vote with respect to such meeting, the issuer shall not be required

to include any proposals submitted by that proponent in its proxy soliciting materials for any meeting held in the following two calendar years.

(2) *Notice and Attendance at the Meeting.* At the time he submits a proposal, a proponent shall provide the issuer in writing with his name, address, the number of the issuer's voting securities that he holds of record or beneficially, the dates upon which he acquired such securities, and documentary support for a claim of beneficial ownership. A proposal may be presented at the meeting either by the proponent or his representative who is qualified under state law to present the proposal on the proponent's behalf at the meeting. In the event that the proponent or his representative fails, without good cause, to present the proposal for action at the meeting, the issuer shall not be required to include any proposals submitted by the proponent in its proxy soliciting material for any meeting held in the following two calendar years.

(3) *Timeliness.* The proponent shall submit his proposal sufficiently far in advance of the meeting so that it is received by the issuer within the following time periods:

(i) *Annual Meetings.* A proposal to be presented at an annual meeting shall be received at the issuer's principal executive offices not less than 120 days in advance of the date of the issuer's proxy statement released to security holders in connection with the previous year's annual meeting of security holders, except that if no annual meeting was held in the previous year or the date of the annual meeting has been changed by more than 30 calendar days from the date contemplated at the time of the previous year's proxy statement, a proposal shall be received by the issuer a reasonable time before the solicitation is made.

(ii) *Other Meetings.* A proposal to be presented at any meeting other than an annual meeting specified in paragraph (A)(3)(i) of this section shall be received a reasonable time before the solicitation is made.

NOTE: In order to curtail controversy as to the date on which a proposal was received by the issuer, it is suggested that proponents submit their proposals by Certified Mail-Return Receipt Requested.

(4) *Number of Proposals.* The proponent may submit no more than one proposal and an accompanying supporting statement for inclusion in the issuer's proxy materials for a meeting of security holders. If the proponent submits more than one proposal, or if he

fails to comply with the 500 word limit mentioned in paragraph (B)(1) of this section, he shall be provided the opportunity to reduce the items submitted by him to the limits required by this rule, within 14 calendar days of notification of such limitations by the issuer.

(B)(1) *Supporting Statement.* The issuer, at the request of the proponent, shall include in its proxy statement a statement of the proponent in support of the proposal, which statement shall not include the name and address of the proponent. A proposal and its supporting statement in the aggregate shall not exceed 500 words. The supporting statement shall be furnished to the issuer at the time that the proposal is furnished, and the issuer shall not be responsible for such statement and the proposal to which it relates.

(B)(2) *Identification of Proponent.* The proxy statement shall also include either the name and address of the proponent and the number of shares of the voting security held by the proponent or a statement that such information will be furnished by the issuer to any person, orally or in writing as requested, promptly upon the receipt of any oral or written request therefor.

(C) The issuer may omit a proposal and any statement in support thereof from its proxy statement and form a proxy under any of the following circumstances:

(1) If the proposal is, under the laws of the issuer's domicile, not a proper subject for action by security holders.

NOTE: Whether a proposal is a proper subject for action by security holders will depend on the applicable state law. Under certain states' laws, a proposal that mandates certain action by the issuer's board of directors may not be a proper subject matter for shareholder action, while a proposal recommending or requesting such action of the board may be proper under such state laws.

(2) If the proposal, if implemented, would require the issuer to violate any state law or federal law of the United States, or any law of any foreign jurisdiction to which the issuer is subject, except that this provision shall not apply with respect to any foreign law compliance with which would be violative of any state law or federal law of the United States;

(3) If the proposal or the supporting statement is contrary to any of the Commission's proxy rules and regulations, including Rule 14a-9 [17 CFR § 240.14a-9], which prohibits false or misleading statements in proxy soliciting materials;

(4) If the proposal relates to the redress of a personal claim

or grievance against the issuer or any other person, or if it is designed to result in a benefit to the proponent or to further a personal interest, which benefit or interest is not shared with the other security holders at large;

(5) If the proposal relates to operations which account for less than 5 percent of the issuer's total assets at the end of its most recent fiscal year, and for less than 5 percent of its net earnings and gross sales for its most recent fiscal year, and is not otherwise significantly related to the issuer's business;

(6) If the proposal deals with a matter beyond the issuer's power to effectuate;

(7) If the proposal deals with a matter relating to the conduct of the ordinary business operations of the issuer;

(8) If the proposal relates to an election to office;

(9) If the proposal is counter to a proposal to be submitted by the issuer at the meeting;

(10) If the proposal has been rendered moot;

(11) If the proposal is substantially duplicative of a proposal previously submitted to the issuer by another proponent, which proposal will be included in the issuer's proxy material for the meeting;

(12) If the proposal deals with substantially the same subject matter as a prior proposal submitted to security holders in the issuer's proxy statement and form of proxy relating to any annual or special meeting of security holders held within the preceding five calendar years, it may be omitted from the issuer's proxy materials relating to any meeting of security holders held within three calendar years after the latest such previous submission:

Provided, that;

(i) If the proposal was submitted at only one meeting during such preceding period, it received less than five percent of the total number of votes cast in regard thereto; or

(ii) If the proposal was submitted at only two meetings during such preceding period, it received at the time of its second submission less than eight percent of the total number of votes cast in regard thereto; or

(iii) If the prior proposal was submitted at three or more meetings during such preceding period, it received at the time of its

latest submission less than 10 percent of the total number of votes cast in regard thereto; or

(13) If the proposal relates to specific amounts of cash or stock dividends.

(D) Whenever the issuer asserts, for any reason, that a proposal and any statement in support thereof received from a proponent may properly be omitted from its proxy statement and form a proxy, it shall file with the Commission, not later than 60 days prior to the date the preliminary copies of the proxy statement and form of proxy are filed pursuant to Rule 14a-6(A) [17 CFR § 240.14a-6(A)], or such shorter period prior to such date as the Commission or its staff may permit, five copies of the following items: (1) the proposal; (2) any statement in support thereof as received from the proponent; (3) a statement of the reasons why the issuer deems such omission to be proper in the particular case; and (4) where such reasons are based on matters of law, a supporting opinion of counsel. The issuer shall at the same time, if it has not already done so, notify the proponent of its intention to omit the proposal from its proxy statement and form of proxy and shall forward to him a copy of the statement of reasons why the issuer deems the omission of the proposal to be proper and a copy of such supporting opinion of counsel.

(E) If the issuer intends to include in the proxy statement a statement in opposition to a proposal received from a proponent, it shall, not later than 10 calendar days prior to the date the preliminary copies of the proxy statement and form of proxy are filed pursuant to Rule 14a-3(a), or, in the event that the proposal must be revised to be includable, not later than five calendar days after receipt by the issuer of the revised proposal promptly forward to the proponent a copy of the statement in opposition to the proposal.

In the event the proponent believes that the statement in opposition contains materially false or misleading statements within the meaning of Rule 14a-9 and the proponent wishes to bring this matter to the attention of the Commission, the proponent promptly should provide the staff with a letter setting forth the reasons for this view and at the same time promptly provide the issuer with a copy of such letter. [Sections 14(a), 49 Stat. 823 and 833; Sec. 20(a) and 38(a), SY Stat. 822 and 841; 15 U.S.C. 78n(a); 78w(a), 791(e), 794(a), 800.20(a), 80a-37(a)]. By the Commission, Commissioner Longstreth dissenting.