

NEW SEC RULES FOR UNIVERSAL PROXY CARDS

WITH JEAN LUTHER, *MEDIANT* AND RON SCHNEIDER, *DFIN*

Dana Barrett: Welcome to The SEC Insider by DFIN. I'm Dana Barrett. And today we're here to talk about the new SEC rules regarding universal proxy cards. Joining me for the conversation are Ron Schneider, who is the Director of Corporate Governance Services for DFIN, along with Jean Luther, who is the Director of Compliance at Mediant. Ron and Jean, welcome.

Jean Luther and Ron Schneider: Thank you.

Dana Barrett: Nice to see you both. I understand there have been some recent updates, believe that just took effect. I think it's September, correct from the SEC Around Universal proxy cards, and Jean, can you explain what this is all about?

Jean Luther: Sure. Back in November or the end of 2021, the SEC finalized a rule on requiring a universal proxy code for any annual meetings where there is a contested election of Directors on non, I should say, for non-exempt election of directors, registered investment companies and business development companies are excluded from this rule, but basically what the rule is requiring is that on the proxy card post the management or registrant and the dissident include the slate of Director nominees for both parties. So on the proxy card coming from the management, they will have their slate as well as the slate of proposed directors that is being put forth by the activist, and vice versa.

In this case, what that allows shareholders to do is they can actually, for the first time, pick and choose across both slates, the nominees that they wish to vote for in the past, they were only allowed to do that if they actually showed up to the meeting in person. And as you said, this rule went into effect for all meetings starting on August 31st of this year.

Dana Barrett: So I guess the obvious question is for people who are not focusing on this day in and day out, how did it work before?

Jean Luther: So I could just start, and then I'll let Ron jump in, because I know he has a lot of firsthand experience on this. But before what would happen is the shareholder would get two different cards. They would get a card from the registrant with their slate of nominees, and then they would get a second card from the dissident with their slate of nominees, and they could really only pick from one slate and whatever card they submitted last, those are the votes that they were cast on their behalf. Ron, I think you can add a lot more color to this, as well.

Ron Schneider: Sure, thank you, Jean. So for the first half of my career I was what's known as a Proxy Solicitor and basically of chasing the vote on behalf of whomever your client was, typically it was management, but in the case of a contested election a proxy fight, and that could be to, you know, oppose a merger or to support a shareholder, sponsor proposal that management doesn't like. But here we're talking about contested director elections. So the majority of people vote by traditionally proxy. The word means substitute. You're not really voting when you sign a proxy card, you're pointing or voting authority, and the manner in which you want your shares voted to a proxy committee. It could be one management person or a group of people, small fine print on the back of the card. And so, as Jean was saying, that's fine, so you could vote for I'm voting for the management slate, oh now I got a later piece of mail from the dissident. I didn't know about this, oh they sound like they're making a great case. I think I want to support them, but they may have been running less than a full slate, a minority slate of directors, so whichever card you returned, and many people would sign and return every card, as Jean said, only the latest they did properly signed card would count. So voting by proxy did not account for mixing and matching it. It wasn't built to do that, and so investors, often institutional investors whose shares were really held at multiple custodians. Therefore they had to vote through multiple street names. It was very, very hard to effect, and many people knowing this behind the scenes reviewing and challenging invalid votes from the other side, as each side would do, and what's known as the challenge period



or snake bit during a proxy fight, which was outside of public eyes, but at the offices of the independent inspector of election, who is running the process, many people attempting logically, you could see their voting intent was consistent, however, under the way, proxies work that's later data that revoked that one, or they're competing proxies to the two different proxy committees. They're off setting each other. Your vote doesn't count at all. So people would inadvertently disenfranchise themselves much more than they knew. So the SEC has been hearing about this for a long time that situation, the desire by some investors not to support one side the other, but to mix and match according to the particular qualifications, diversity, whatever it is that attracts them to particular nominees. They want to vote by nominee, not just by slate. So that's exactly what this is meant to address.

Dana Barrett: Okay, so I think we're kind of dancing around the most basic question here, which is what is a universal proxy card, and you talked a little bit about it, Jean, in terms of now you know all of the choices are up on this proxy card, but can you dig into it a little bit more? What did they look like, how different are they physically, what's the difference?

Jean Luther: Well, I think I will show some examples here. But basically what's going to happen is the management or registrant side is going to present a proxy card, and if you still see on the proxy card itself there will be a slate of their nominees, and directly below that there is going to be a slate of the registrant nominees. The rules require that there are certain things that need certain formatting that needs to be followed, so the names need to be in alphabetical order, they need to separate the two slates. They need to totally identify the card. That is their card, so it needs to say at the top that it's the management card, or it needs to say boldly, that is the dissident card, and you'll see on the on the examples that we're presenting. There's a management and a dissident card that that's how the layout is going to look. The formatting should be the same for both slates. But there is some flexibility on how you design the card, but each side will present a card, so a shareholder will still get two cards or potentially get two cards. They will just see both slates on each card, probably in a different order.

Dana Barrett: So does this make it more clear, not to vote twice, because now you've got all the information.

Jean Luther: I don't think it makes it more clear not to vote twice, because you're still getting two cards, but on both cards, you're going to have the same choices.

Dana Barrett: And if you do vote on both cards, does one get disqualified?

Jean Luther: It's always going to be last in. It will be the both that counts.

Dana Barrett: Okay, so that has not changed.

Jean Luther: Correct.

Dana Barrett: Okay. So if you get the second card, you could sort of change your mind and pick different people and send it in.

Jean Luther: Yes, and I mean even you can always change your mind up until all the voting platforms will allow you to change your mind. If you go online, you can change your mind up until the voting cut-off. If you actually mail in a physical card, obviously it will be the last card that is received physically by now.

Dana Barrett: Okay. Interesting. So what other requirements are contained in the new SEC Rule?

Jean Luther: Okay, I'll start, and I'll let Ron jump in on this one as well. So there are a few interesting points that are included in the rule. One is that the determination of a bona fide nominee not only applies to anyone who's named in any proxy statement, so now you don't have to be named in just one proxy statement, or the registrant proxy statement. You can be named either in the register and proxy statement or in the dissident, so that opens up the opportunity there for the nominees. The dissidents need to notify the registrant.

Sixty days prior to the one-year anniversary of the previous year's meeting of their intent to solicit proxies and the listing of the nominees that they're going to be putting forward. The registrant then must notify the dissident 50 days prior to the annual anniversary of the previous meeting, the list of nominees that they are putting forward. The dissident needs to solicit 67 percent of the outstanding voting power of shares that are entitled to vote at that meeting.



Also, from what I have heard, there are some people that feel like that's a pretty low bar that can be easily attained just by the dissidents simply soliciting institutional investors as opposed to actually reaching out to all investors, which you know, we're going to see how that plays out this year. And the dissident has to include their intention to solicit the minimum amount of shareholders in their proxy statement. Ron, did I forget anything, anything else you want to add?

Ron Schneider: No, those are the major ones. Now, what's to be determined with any new law, and the uncertainty and how it's going to work. There is one law that in my experience has always been true, and that's the law of unintended consequences. So we are yet to see how that will roll out, and when you're talking about contestant activity, you're talking who the participants are. Often, I mean it's smart, savvy, fast money investors. Okay, it's hedge funds. This activists, it's others, they are very well advised. They know right where the rule goes, and right where the line is, and just a little behind it beyond it. So you can expect, and I'm not, you know, call on this evil or anything. But there will be either delivered or inadvertent efforts to you know, game. The system in terms of its intent. So, for example, a dissident says it gives timely notice to the company of their intent to solicit and names or nominees, and said, oh, yes, and we will. Yeah, we'll take care of that two-thirds part. You know who's going to police whether they actually followed through and did furnish their proxy statement subsequently to a sufficiently wide body of the shareholder base we're going to see. I think you know the typical recourse is litigation, all right. There's going to be plenty of that in many of these situations, you know both Jean, I think, and myself. I've been hearing different speculation about what's just going to do to the level of activism, and I'll tell you, already on top of the traditional economic activism, performance activism, traditional governance activism there has over the last two years been an increased wave of what people are calling ESG activism where it could be criticism over the company's pace or strategy of change in light of ESG consideration is not satisfactory.

Now that may result in a traditional contest. Well, because they're failing on ESG, that's another reason why we need to get new directors in there, that kind of thing. The other is that it is calculated to make it easier for investors, that's what it's all about the picking and choosing to both the way they want. And therefore it may make it more likely that a dissident may not get their whole slate, but they may get one director on representation on the board with the greater opportunity to get representation on the board. It won't be surprising to see a greater incidence or frequency of contests, plus because of the later dated card going away, I mean only as Jean clarified, only the latest stated, properly executed, universal ballot will rule. So you can change your mind along the way. But you don't have to keep mailing a new proxy card with every subsequent mailing. I've been in proxy fights where there were 11 mailings from both sides—there's a lot of printing, there's a lot of mailing, there's a lot of postage now. Sure a lot of its electronic now. But to this date, the hard copy in the mail overall is still the best way to generate retail, individual voting support, not institutional. So in many close contests, if the dissident is really interested in taking control, they're going to have to solicit the majority of the shareholder base.

The company, to defend itself is always going to solicit 100 percent of its required to solicit everyone on at least the initial mailing. They can do follow-ups more selectively. So I think it's highly likely it's going to increase the frequency, the range of topics, the effectiveness, and lower the cost of contested elections. And then add to it the uncertainty. How's it going to play out? How much more litigation around who followed the rules properly? Who didn't. Let the games begin.

Dana Barrett: So what does this specifically mean for DFIN clients?

Ron Schneider: Thank you, Dana. So we've been talking about what universal ballot is. We start at the beginning. How's it different from the past and everything. So what do you do? So there's an environment out there now, where, whether you, as a company or know that you are a specific target. There's no 13D, haven't heard of an activist? Anything like that? Everyone is in this environment of heightened activism. Okay, so what is the traditional advice when you know you may face a contested election? When you are caught flat footed. If you are hit with a proxy by all of a sudden? Unfortunately, your traditional budgets go out the window. You put yourself largely in the hands of your outside council. They recommend a range of contest specialists from solicitors to PR firms and others. And control of the board is at stake and direction of the company is at stake. The stakes are very high, and so, what are you doing? You follow the advice. Well, gee! Start engaging with your investors. Now you don't have relationships with them.



We'll start building them now. Oh, you have a kind of playing traditional proxy that doesn't really go much for the rule 14A doesn't really show the strengths of the current board, doesn't show its diversity, doesn't show the range of skills and qualifications, including competencies, to handle the new requirements of ESG oversight. Well, you're going to be scrambling to tell that story once the bell goes off. So what can you do now? You can't control. If you will be entirely. If you will be subject to a future fight, you can start improving your board story. Now you and your copy the governance and nominating committee can be looking with great sense of urgency, or are there any gaps in the board skill set is, are we kind of been slow on refreshment? Is the bail as a board, looking a little, stale mail and pale, as some people say? Are there some critical skill sets that we want to fill? Well, maybe then you pump the gas and intensify that effort. You want to fill any gaps in your board skill set before a third party. A dissident comes in. It does for you by telling that superior story, you may actually dissuade the dissidents from selecting you as a target, and they may choose, well, this company's got a pretty good story, and I don't know what we're going to attack here. The performance is good, their board is good, their disclosures are good, and maybe there's a softer target. And so, through our guide to effective proxies as well, which each year catalogs some of the most interesting and creative treatments from our client proxies. It's now sliced and diced into 38 different sections, topics and features. About a third of them are directly board related. So we would say, take a look at your current disclosures. Right. Can your board, bios be beefed up, you're not including photos yet. People want to see who the dissidents are. They want to see who the incumbents are that they're supposed to support. Talk about the board leadership structure. Why it's right for the company, whether it's combined, share CEO with a lead independent director or separate positions. Why is it right for your company?

Talk about the current diversity on the board, be it gender, ethnicity race, geographic and most important, the breadth of skills and qualifications, and why they're right for the current and foreseeable needs of the company, including in this new ESG-focused environment. Highlight the board mix of skills. There must be some kind of a skills matrix, maybe not as detailed as your internal, but a board planning tool, but that you're willing to put out there publicly, as in more and more companies are to highlight the breadth and depth of the expertise on your board. Talk more about the processes that will lead to further board refreshment, board evaluations direct to recruitment and refreshment. Take a look at these things now, because what if you are hit with an activist situation? That's what you're going to be scrambling to try to do so don't wait, start now. We spent a lot of time and effort, not just on putting together a tool like the guide. That is the deficiency tool for companies and our advisors. But we have at least 200 one-on-one conversations with individual clients about their needs, their goals or objectives. Where then we help them to spruce up those aspects of their proxy, governance and sustainability store in the next proxy. So if you're not engaging with your investors, get started now. If your proxy is behind the level of your current peer company proxies, get working on that now.

Universal proxy is a new catalyst. The advice is tried and true. Take advantage of the time. Now do it your way before your hand is forced.

Dana Barrett: Absolutely. Well, thank you guys both very much, Ron and Jean. I appreciate your time. This has been the SEC Insider by DIFN. We'll see you next time.