

EXCLUDING A SHAREHOLDER PROPOSAL? NOT SO FAST...

Nov 12, 2021

The SEC's Division of Corporation Finance recently published [Legal Bulletin 14L \(CF\)](#) (the "Bulletin") providing updated guidance on excluding shareholder proposals under Rule 14a-8 under the Exchange Act. Specifically, the Bulletin addresses the circumstances under which a company may exclude a shareholder proposal from its proxy materials either because it falls within the "ordinary business exception" of Rule 14a-8(i)(7) or the "economic relevance exception" of Rule 14a-8(i)(5). The Bulletin rescinded previously issued Staff Legal Bulletins [14I](#), [14J](#) and [14K](#) after a review of Staff experience applying the guidance in them. The Bulletin's overall effect will limit the circumstances under which companies may exclude shareholder proposals. As a result, we expect to see more shareholder proposals concerning climate change and other ESG-related issues in the 2022 proxy season.

Ordinary Business Exception Tightened. Under the ordinary business exception, a company may exclude from its proxy materials a proposal that relates to the company's ordinary business operations. The premise is reasonable – decisions regarding these matters should be in the hands of management or the board as part of their oversight of the company's day-to-day operations and not in the hands of "overreaching shareholders."

Expansion of Significant Social Policy Test. A company cannot exclude a proposal under the ordinary business exception if it concerns a "significant social policy." In the past, in determining whether a proposal involved such a policy, the Staff painstakingly analyzed the extent to which the social policy raised in the proposal affected and was relevant to the particular company. If the Staff found an insufficient nexus between the policy and the company, then no matter how impactful the issue (e.g., climate change), the proposal could be excluded.

Under the Bulletin, moving forward, the Staff will focus solely on the significance of the social policy itself and will no longer conduct a company-specific analysis. If the Staff finds that proposals raise issues having a "broad societal impact, such that they transcend the ordinary business of the company," then companies cannot exclude them under the ordinary business exception.

The Staff will no longer expect a board analysis for the consideration of a no-action request under this policy exception, as had been introduced as a requirement in the superseded guidance.

Narrowing of Micromanagement Exclusion. A company can exclude a proposal if it would result in the shareholders' micromanagement of the company by "probing too deeply into matters of a complex nature upon which shareholders, as a group, would not be in a position to make an informed judgment." The Bulletin provides that, in the past, the Staff may have defined micromanagement too broadly such that any limit on management or the board was deemed to constitute impermissible micromanagement.

Moving forward, the Staff will focus on the level of "granularity" sought in the proposal and whether and to what extent the proposal inappropriately limits the discretion of the board or management. Specific methods, timelines and detail do not necessarily amount to micromanagement, and a proposal should include detail that will allow "investors to assess an issuer's impacts, progress towards goals, risks or other strategic matters appropriate for shareholder input." In deciding whether a matter is too complex for shareholders, the Staff may consider the "sophistication of investors generally with regard to the subject matter of the proposal, the availability of data and the robustness of public discussion and analysis on the topic." In the past, proposals that included timeframes or targets to address climate change could be excluded. Going forward, however, the Staff would not concur with such an exclusion as long as the proposal allows management and the board discretion as to how to achieve the specific goals.

Economic Relevance Exception Limited by Social Policy Considerations. Under the "economic relevance exception," a company may exclude from its proxy materials a proposal that "relates to operations which account for less than 5 percent of the company'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 company's business." In the past, the Staff applied the quantitative thresholds when determining whether a proposal could be excluded, and, if the relevant business fell below the thresholds, then a company could exclude the proposal.

Moving forward, the Staff – presumably focusing on the third prong of the test – may determine that a proposal not meeting the thresholds may not be excludable if it raises "issues of broad social or ethical concern related to the company's business."

The Staff also will no longer expect a board analysis for the consideration of a no-action request under the economic relevance exception.

Other Matters Covered. The Bulletin also includes guidance regarding (1) the use of graphics and images in requests for Rule 14a-8 no-action letters, (2) proof of ownership letters that accompany

shareholder proposals and (3) the use of email for the submission of proposals, delivery of notices of defects in shareholder proposals and responses to notices of defect.

Dissenting Commissioners. SEC Commissioners Hester Peirce and Elad Roisman issued a [statement](#) asserting, among other things, that the new Bulletin does not fill the void left by the rescinded bulletins; does not sufficiently explain the problems with the rescinded bulletins; and makes changes to the application of the ordinary business and economic relevance exceptions that will make them even harder and more time-consuming to apply.

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R. Randall Wang

St. Louis

randy.wang@bcplaw.com

[+1 314 259 2149](tel:+13142592149)

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