

The SEC's universal proxy proposal: How it affects Canadian companies and investors

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The U.S. Securities and Exchange Commission (SEC) has proposed amendments to its proxy rules that are designed to allow shareholders using the proxy system to vote for their choice of a combination of candidates in a contested election for directors, rather than being limited only to the candidates on either a management proxy or dissident proxy. The proposed changes could make it easier and less costly for dissident candidates to be elected to corporate boards, which could have ripple effects on corporate governance practices and negotiating strategies for activists. Use of a universal proxy would require the dissident to provide advance notice of its nominees and incur the cost of preparing dissident proxy materials and sending those proxy materials to potentially more shareholders than it would otherwise solicit. The proposed rules remain open for comment until January 9, 2017.

Canadian implications

The SEC's proposed rule changes would not have a direct impact on the vast majority of Canadian companies, even if they are also public in the United States, because most Canadian companies qualify as "foreign private issuers" under the SEC's rules and are therefore not subject to the SEC's proxy rules. However, a universal proxy has been successfully used in at least one Canadian proxy contest (Pershing Square's dissident campaign against CP Rail), the Canadian Coalition for Good Governance has previously expressed support for the use of universal proxies, and the close integration of Canadian and U.S. public markets often leads to adoption of similar requirements under Canadian securities laws. The requirement to use a universal proxy would generally depend on the company receiving advance notice of a dissident's director nominees no later than 60 days prior to the anniversary date of the previous year's annual meeting. It is noteworthy that the SEC's proposed deadline does not align with the deadlines under advance notice provisions for director elections as commonly adopted in Canada, which, for example, generally require notice to be provided at least 30 days prior to the meeting date.

Canadian-based investors in companies subject to the SEC's proxy rules may find that they have more choice for whom they can elect as directors without incurring the time and cost currently involved in vote-splitting for contested U.S. public company director elections.

The current proxy rules: my slate or the highway

The SEC's goal is to allow shareholders voting by proxy to choose among director nominees in an election contest in a way that more closely reflects the choice they could make by voting in person at a shareholders' meeting. Shareholders voting in person in corporate contested elections with competing slates of director nominees are able to choose from among all of

the properly nominated candidates. Shareholders voting by proxy, however, are limited to the selection of candidates listed on a soliciting party's proxy. To further complicate matters, under state law, a later-dated proxy card generally invalidates any earlier-dated proxy card, effectively limiting a shareholder to voting on a single proxy card. The end result is that shareholders voting by proxy (which is how U.S. corporate elections are usually decided) are typically limited to voting either only for the company's nominees or only for the dissident's nominees. If shareholders wish to vote for a combination of nominees selected from each slate, they generally must either show up at the shareholders' meeting in person or send a representative to the meeting. In some cases, proxy solicitors or similar service providers may make arrangements for one or more individuals to attend a meeting on behalf of certain shareholders in order to facilitate split-ticket voting. These options can be time consuming and expensive.

The proposed changes: choose your own adventure

The SEC's proposed amendments would require the use of a universal proxy in all contested elections with competing slates of director nominees. While each party in the contest would continue to use its own proxy card to solicit votes for its director candidates, each proxy card would be required to include all candidates properly nominated by anyone. Though all proxy cards would be required to include the names of all nominees, a proponent of nominees would not be required to provide background information about its opponents' nominees in its own proxy statement. The SEC's proposed amendments would impose certain other related requirements in the case of contested elections with competing slates of nominees:

- In order to provide advance notice of the requirement to use a universal proxy, dissidents would be required to provide the names of the nominees for whom they intend to solicit proxies to the company — no later than 60 days before the anniversary of the previous year's annual meeting date — and the company would have to provide notice of its nominees to dissidents no later than 50 days before that anniversary date.
- To provide shareholders timely access to information about all nominees, a dissident would be required to file its definitive proxy statement with the SEC by either 25 days prior to the meeting or five days after the company files its definitive proxy statement (whichever is later).
- Dissidents would be required to solicit the holders of shares representing at least a majority of the voting power of shares entitled to vote on the election of directors.
- There would be presentation and formatting requirements for universal proxy cards to help ensure that the names of all parties' nominees and the total number of nominees for whom a shareholder can vote are clearly and fairly presented.

The impact of universal proxies

Universal proxies would result in direct cost savings for shareholders who wish to vote for a combination of some candidates proposed by the company and some proposed by the dissident and who otherwise would incur the associated additional costs of attending in person or hiring a representative, to be able to vote for their preferred combination of nominees instead of being forced to choose either the company slate or the dissident slate. However, it is not clear whether activists will conclude that the advantage of using universal proxies outweighs the timing and cost requirements of complying with the proposed rule. Should the use of universal proxies become widespread, they may have broader impacts on corporate governance and the relationship between shareholders and management. For

example, enabling split-ticket voting could lead to a greater number of boards that are composed of a mix of company-nominated and dissident nominated directors, which could have either a positive or negative impact on the board's decision-making.