

# Shareholder Engagement and Proxy Access

November 10, 2016

# Panelists

- **Patrick Davidson**  
Vice President Investor Relations, Oshkosh Corporation
- **Rick Grubaugh**  
Senior Vice President, D.F. King & Co.
- **Eric Nelson**  
Senior Vice President and Associate General Counsel, Fiserv, Inc.
- **Patrick McGurn**  
Special Counsel, Institutional Shareholder Services
- **John K. Wilson**  
Partner, Foley & Lardner LLP

# SHAREHOLDER ENGAGEMENT

# Shareholder Engagement Background

- Shareholder engagement traditionally limited to earnings calls and annual meetings
- No longer adequate—today's investors demand more attention
- Engagement can benefit both the company and its shareholders:
  - The best boards will seek self-awareness and feedback from shareholders
  - Shareholders who feel engaged are more likely to offer long-term support

# ISS as Driver of Engagement

- ISS considers directors' responsiveness to shareholder input as one of its four fundamental principles when determining votes on director nominees
- If a company's previous say-on-pay vote received the support of less than 70% of votes cast, ISS will consider the company's response when evaluating its case-by-case votes on compensation committee members
- If a board amends the company's bylaws or charter without shareholder approval in a manner that materially diminishes shareholders' rights or could adversely impact shareholders, ISS will consider disclosures by the company of any significant engagement with shareholders regarding the topic when determining its vote

# ISS as Driver of Engagement

- ISS will consider a company's track record of responsiveness to, and disclosure of engagement with, shareholders as a factor in its votes on other topics, including:
  - Advisory votes on executive compensation (management say-on-pay)
  - Management proposals to ratify a poison pill to preserve net operating losses
  - Management/shareholder proposals to restrict or prohibit shareholders' ability to act by written consent, or to call special meetings
  - Management/shareholder proposals on proxy access, including the terms thereof

# No Definitive Approach to Engagement

- There is no one “right” way to do shareholder engagement—each company and its shareholders are unique
- Vanguard Group stressed this point in a 2015 letter to the board chairs or independent directors of its largest holdings:
  - *“While we advocate for shareholder engagement, we don’t presume to know what the optimal structure for engagement looks like for your board. To be sure, there is no one-size-fits-all engagement program. We encourage you to speak to your board about engagement, and create a process that meets your needs and those of your shareholders.”*

# Structures for Engagement: Shareholder Engagement Policy

- Not required, but a growing number of companies are voluntarily adopting policies on shareholder engagement
- Adopting a policy has a number of benefits:
  - Commits the board; facilitates constructive engagement
  - Governs communication with shareholders
  - Encourages accurate, consistent, regular communication
  - Increases likelihood of Regulation FD compliance
- Shareholder engagement policies typically address:
  - Board philosophy regarding shareholder communication
  - Division of board and management responsibilities
  - Frequency, method and topics of communication
  - Who will be allowed to participate – from the board, from management and from shareholders

# Structures for Engagement: Shareholder Engagement Committees

- Some boards have begun to create standing committees devoted to managing the shareholder engagement process
- ISS's proxy voting guidelines generally support proposals to establish a shareholder engagement committee
- Shareholder engagement committee members need not be independent, but independence will enhance credibility with shareholders
- As with other board committees:
  - A written charter is recommended
  - The board should seek to appoint members with the appropriate mix of skills, experience and availability for the task of engaging key shareholders

# Considerations, Preparation and Process for Shareholder Engagement

- Start by becoming familiar with your top shareholders, including:
  - What their voting guidelines are, and how they may vary from proxy advisory firms' guidelines
  - Who makes the voting decisions at each shareholder
- Understand your key shareholders' "hot button" issues
  - Benchmark your company's position on these issues against industry peers
  - Attend conferences and other events where shareholder representatives may speak on these issues
  - Be prepared to ask questions and engage in dialogue
  - Avoid boilerplate or giving a one-size-fits-all roadshow

# Considerations, Preparation and Process for Shareholder Engagement

- Determine who will speak for the company
  - Shareholder engagement policy will help to establish this
  - CEO/CFO typically not well suited; more often, the general counsel, corporate secretary or director of investor relations will be better positioned as the initial point of contact
  - Directors may be involved, depending on the issues being discussed (e.g., executive compensation) or if requested by the shareholder
- Promote ongoing communication
  - Year-round engagement indicates a willingness to work with shareholders
  - Shareholders with numerous holdings often don't have time or the resources to engage during proxy season
  - The “off season” (late summer/early fall) may offer better opportunities for engagement

# Considerations, Preparation and Process for Shareholder Engagement

- Be prepared to follow up and respond to shareholders' concerns
  - Engagement should not be a series of isolated, standalone encounters
  - Carefully consider shareholders' concerns and assess whether changes are warranted
  - If changes are made, a coordinated effort to publicize those changes should typically follow
  - If changes are not made, reengage with the shareholder to ensure the shareholder appreciates the company's rationale and to reaffirm the shareholder's input is valued
- Disclose shareholder engagement activities in the company's proxy statement

# Current Trends/Statistics in Shareholder Engagement

- 64% of companies report they engage with shareholders in some form<sup>(1)</sup>
- Directors are involved in engagement 38% of the time<sup>(1)</sup>
- Most popular topics of discussion during engagement sessions include:<sup>(1)</sup>
  - Compensation (47%)
  - Proxy access (18%)
  - Strategy (11%)
  - Board structure (9%)
  - Performance/operations (9%)

# Current Trends/Statistics in Shareholder Engagement

- Companies and shareholders tend to view engagement differently:<sup>(2)</sup>
  - Companies tend to see engagement in terms of isolated incidents: 66% of companies say engagement typically lasts a week or less (sometimes as little as a single phone call)
  - Shareholders tend to view engagement in the bigger picture: 61% of shareholders say their engagement typically lasts more than one month (and often over a period of several years)
- Approximately 60% of companies and 85% of shareholders say that more directors are taking part in shareholder engagement than was the case three years ago<sup>(2)</sup>

# Current Trends/Statistics in Shareholder Engagement

- Approximately 60% to 70% of both shareholders and companies agree that engagement is increasing<sup>(2)</sup>
- Since 2011, the number of S&P 500 companies disclosing shareholder engagement in their proxy statements has doubled<sup>(3)</sup>
- Among shareholders surveyed, the top four outcomes that shareholders viewed as a successful engagement were:<sup>(2)</sup>
  - Additional company disclosure or specific changes in company policies/practices
  - Company commitment to engage on issues of concern in the future
  - Constructive dialogue on specific issues of concern
  - Establishment of dialogue, even if contentious, between shareholders and the company

# Current Trends/Statistics in Shareholder Engagement

- Sources for statistics on the preceding slides:
  - (1) PricewaterhouseCoopers, “Director-shareholder engagement: the new imperatives,” June 2016
  - (2) Institutional Shareholder Services, “Defining Engagement: An Update on the Evolving Relationship Between Shareholders, Directors and Executives,” April 10, 2014
  - (3) Equilar, “Shareholder Engagement: Adapting to a New Era of Investor Relations,” August 3, 2016

# PROXY ACCESS

# Proxy Access Background

- “Proxy access” is the ability of shareholders to use the company proxy statement (and card) to propose their own director candidates to compete in part with management’s slate
  - Comparable to a Rule 14a-8 shareholder proposal, but allowing director candidates instead (e.g., 12 candidates for 11 seats)
    - Otherwise, to advance a competing nominee, a shareholder must circulate its own proxy statement and solicit votes using its own proxy card
  - Typically implemented through a Board-approved bylaw amendment
- The SEC had adopted a rule to allow such access
  - A court overturned the rule, but the door was left open for shareholder proposals on the subject

# Proxy Access Background

- Subject roared back in 2015 after fairly quiet 2013 & 2014; still strong in 2016
  - NYC Comptroller & Boardroom Accountability – 75 proposals in 2015; 72 in 2016
  - The usual proponents (including Chevedden) were on the bandwagon in 2016, too
  - 91 shareholder proposals voted on in 2015; over 80 to date in 2016
- A mainstream shareholder proposal is likely to pass if a company has no good counterarguments and no large shareholder that opposes proxy access

# Proxy Access Trends

- Proxy access will continue to be the current governance hot topic
- Over 40% of S&P 500 companies have now adopted proxy access
  - Proxy access expected to become a majority practice among S&P 500 companies in 2017
- Over 60 companies have adopted proxy access on their own without a known shareholder proposal
- The number of companies receiving shareholder proposals requesting the adoption of proxy access continues to substantially increase
  - 115 proposals for 2015 and over 200 proposals for 2016
  - This trend is expected to continue for 2017
  - Proposals typically request 3% ownership for 3 years and up to 25% of the board and often provide an unlimited number of shareholders can aggregate as a group
  - Difficult to exclude a proposal from the proxy statement under current SEC no-action letters

# Proxy Access Trends

- Investor support of proxy access continues to increase and ISS continues to recommend in favor of proxy access
  - The average support in 2016 for proxy access proposals at companies that did not adopt proxy access was significantly higher than at companies that did adopt proxy access
  - ISS recommend in favor of virtually all proxy access shareholder proposals in 2016 where a company had not previously adopted a proxy access bylaw or had a competing management proposal
- Certain proponents targeting companies that received a shareholder proposal in 2016 and adopted proxy access but not on terms to the satisfaction of the proponent – “fix proxy access” shareholder proposals
  - At least 9 proposals submitted in 2016 and more expected in 2017
  - For example, requests to remove limits on shareholder group aggregation and renomination of nominees who did not receive a minimum percentage of votes in the prior year

# Proxy Access Trends

- Institutional investors, proxy advisory firms such as ISS and companies adopting proxy access are developing a consensus on terms of proxy access that are generally acceptable to all
  - First tier key terms of 3% ownership for 3 years with the ability to nominate the greater of 2 nominees or 20% of the board with a nominating group size of 20 shareholders are now standard
  - Second tier key terms are also becoming more standard with proxy access adoptions during 2016
- To date, proxy access has not been used at the companies that have adopted it to nominate and elect shareholder candidates to a board
  - But, as more companies adopt proxy access, it becomes more likely that it will be used

# Factors in Favor of Voluntarily Adopting Proxy Access

- Adoption may deter a shareholder proposal, and voters seem to support a mainstream company-adopted bylaw in face of shareholder attack
- Companies generally can adopt on its own terms through Board action, including through bylaw language
- Key terms & other important terms seem to be more settled; opportunity to stake claims on remaining terms
- Some governance points for adopting
- Potential basis to exclude shareholder proposal through SEC process
- Proxy access right may not get much use anyway
  - True activists unlikely to use due to conditions and limitations; large shareholders will likely assert direct pressure

# Factors Against Voluntarily Adopting Proxy Access

- If shareholders object to terms, they will attack bylaw with a proposal anyway
- If a company receives a proposal, it can still “voluntarily adopt” on its terms before a vote on the proposal to facilitate three possibilities:
  - May be able to negotiate withdrawal of shareholder proposal
  - May be able to exclude the shareholder proposal through SEC process
  - Should be able to defeat the shareholder proposal if consistent with recent trends
- Some important terms are not yet settled
- So far, no governance “demerits” for not having proxy access