

March 1, 2017

## REITs and Proxy Access

By: Michael Hermsen and Laura Richman

Proxy access initiatives made significant inroads during the last two proxy seasons. Much of the impetus for proxy access came from the Boardroom Accountability Project campaign launched by the Comptroller of New York City and the New York City Pension funds, which submitted proxy access proposals to 75 companies during the 2015 proxy season and to 72 companies for the 2016 proxy season. The proxy solicitation and corporate advisory firm, Alliance Advisors, reported that over 200 proxy access resolutions were submitted by shareholders during the 2016 US proxy season and that, as of February 1, 2017, 379 companies had adopted proxy access, of which 22 were real estate investment trusts (“REITs”).<sup>1</sup>

According to Alliance Advisors, through July 1, 2016, shareholders voted on 79 shareholder-sponsored proxy access proposals, receiving on average 51.1 percent support from shareholders. Of these proxy access proposals, 41 (representing 52 percent of the total) received majority votes in favor. This compares to 91 voted on shareholder-sponsored proxy access proposals in 2015, receiving an average 54.8% support from shareholders and 55 of which received majority votes in favor.<sup>2</sup> The difference between the number of proxy access proposals submitted by shareholders and those actually voted on is due to negotiated withdrawals and voluntary adoptions by companies.

Beginning early in the 2016 proxy season, the Staff granted a series of no-action requests to allow companies to exclude from their proxy statements shareholder proposals requesting the adoption of proxy access where the companies had adopted proxy access provisions that they claimed “substantially implemented” such shareholder proposals before their annual shareholders meetings. The Staff agreed that the companies had substantially implemented the shareholder proposals where they had adopted provisions granting proxy access to shareholders who held three percent of the company’s stock for three years, even though the provisions adopted did not completely mirror the other terms of the shareholder proposals. In these cases, the Staff was satisfied that the proposals that the companies adopted achieved the “essential objective” of the proxy access provision requested by the shareholder proposals.<sup>3</sup>

Substantially all of the US proxy access provisions that have been adopted use a three percent ownership/three-year threshold, comparable to the threshold that the SEC adopted in its original proxy access rule, which was vacated by court action. Other typical terms include requiring shareholders to have full voting and economic ownership in order to use proxy access and allowing aggregation by groups of not more than 20 shareholders to reach the designated threshold. It is also common to limit the number of proxy access nominees to 20 percent of the board, but often with a minimum of two nominees. Although there are quite a few other details on which proxy access provisions vary, to a large degree there have been a sufficient number of US proxy access provisions adopted that there is a growing consensus as to which variations are viewed as “market.”

A comparison of the core proxy access provisions adopted by companies in general and those adopted by REITs shows no significant difference.

**Core Provision Comparison**

<b>Companies in General<sup>4</sup></b>	<b>REITs</b>
Percentage ownership threshold	
3% (99%) 5% (1%)	3% (100%)
Years of ownership	
3 (100%)	3 (100%)
Number of holders that may make up a group	
20 (91%) 25 (4%) 10 (1%) Other (4%)	20 (77%) 25 (13%) 10 (5%) 5 (5%)
Number of directors that may be elected by proxy access	
Greater of 2 or 20% (67%) 20% (20%) Greater of 2 or 25% (7%) 25% (7%)	Greater of 2 or 20% (46%) 20% (27%) 25% (18%) Greater of 2 or 25% (9%)

Companies that do not allow for proxy access may receive shareholder proposals requesting that proxy access be adopted. Such companies may want to consider having one on “the shelf” in case they receive a shareholder proposal and would then be in a position to act relatively promptly or adopting their own proxy access provisions in order to incorporate the detailed aspects in a manner that they think makes sense, while at the same time satisfying the essential objectives test necessary to persuade the Staff that the shareholder proposals have been substantially implemented.

Companies that have already adopted proxy access provisions may nevertheless receive proxy access shareholder proposals that request amendments to specific features of their existing provisions that certain shareholders find objectionable (so-called “fix-it proposals”). Among the provisions shareholders are seeking to amend in existing proxy access proposals include:

- Increasing the number of proxy access nominees to the board of directors to the greater of 25 percent or two nominees;

- Eliminating the cap on the number of shareholders that can aggregate their shares to achieve the required three percent ownership threshold for proxy access nominations;
- Eliminating renominations based on the number or percentage of votes received in any election;
- Permitting loaned securities to be counted toward the ownership threshold in certain circumstances;
- Eliminating any requirement to continue to hold shares after the meeting; and
- Eliminating any ability of the board to amend a proxy access bylaw.

When a shareholder requests particular amendments to a proxy access provision, a company should expect that it will be more difficult to convince the Staff that a proposal has been substantially implemented by an existing proxy access provision that does not contain the revisions that are being specifically requested. To date the Staff has been reluctant to allow companies to exclude “fix-it proposals” even where the Staff would allow the exclusion of a shareholder proposal from a company’s proxy statement if it related to adoption of a proxy access provision on similar terms. Where the Staff has allowed a company to exclude a “fix-it proposal,” it appears that the Staff is focusing closely on the facts and circumstances presented by companies in reaching their conclusion, including such things as whether a company has 20 shareholders whose aggregate holdings could meet the ownership threshold.<sup>5</sup>

It will be important for companies to monitor how shareholders view the “fix-it proposals” during the upcoming proxy season. The results of these proposals will provide valuable information for companies trying to decide what terms to include when adopting a proxy access bylaw or for companies trying to decide how to respond to their own “fix-it proposal.” Accordingly, despite the many voluntary adoptions of proxy access bylaw provisions during the past year, proxy access is likely to be an area of continued focus by companies and shareholders during the coming year.

---

<sup>1</sup> Most recent listing and core terms available at <http://allianceadvisorsllc.com/wp-content/uploads/2017/02/Companies-with-Proxy-Access-2-1-17.pdf>.

<sup>2</sup> Available at <http://allianceadvisorsllc.com/wp-content/uploads/2016/07/Alliance-Advisors-Newsletter-July-2016-2016-Proxy-Season-Review.pdf>.

<sup>3</sup> See, e.g., SEC no-action letter issued to Amazon, Inc. dated March 3, 2016, available at <https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2016/jamesmcritchieamazon030316-14a8.pdf>.

<sup>4</sup> See footnote 1 for more information.

<sup>5</sup> For examples of letters reaching opposite conclusions where the proponent in each case sought to amend a proxy access bylaw to increase the number of shareholders to 50 who could be aggregated for purposes of meeting the ownership threshold, see, SEC no-action letter issued to Citigroup Inc. dated February 10, 2017 available at <https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2017/kennethsteinerCitigroup021017-14a8.pdf> and SEC no-action letter issued to Eastman Chemical Company dated February 14, 2017 available at <https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8/2017/johncheveddeneastman021417-14a8.pdf>.