January 26, 2021

The Hon. Allison Lee
Acting Chair
U.S. Securities and Exchange Commission
Division of Corporation Finance
100 F Street, N.E.
Washington, D.C. 20549

RE: SEC Rule 14a-8 no action process and climate change

Dear Acting Chair Lee,

Congratulations on assuming the role of Acting Chair of the SEC. The undersigned organizations deeply appreciate your leadership, including on issues of climate change. We are writing to ask you to put reform of recent SEC no-action process developments on the agency's agenda as an action item on climate change.

As you know, President Biden issued an Executive Order on January 20 entitled *Protecting Public Health and the Environment and Restoring Science to Tackle the Climate Crisis*. Consistent with the impetus of that Executive Order, we hope that you will set a climate change agenda for the agency, including the issues that investors have flagged on the no-action process and Staff Legal Bulletins. We believe this would be consistent with the principles and views expressed in your November 5, 2020 speech "Playing the Long Game: The Intersection of Climate Change Risk and Financial Regulation."

Some of us have written to you previously with suggestions for SEC actions on climate change. The enclosed report of the Shareholder Rights Group and Interfaith Center on Corporate Responsibility was presented to the Biden Transition Securities Regulation Team. It highlights the need for redirection of the no-action process and repeal of Staff Legal Bulletins 14I, 14J and 14K to re-enable shareholders to ask their investee companies to improve disclosure and performance on climate change. In addition, USSIF has included this in their policy recommendations for the new Administration.

Shareholders concerned with climate risk need the opportunity to ask their portfolio companies to increase the scale and pace of their responses to climate change. Yet we are aware of currently pending no-action requests[1] on climate change

[1] For instance, a proposal at Valero asks the company to evaluate its executive remuneration policies against the Climate Action 100+ benchmarks backed by investors with $52 trillion of assets under management. Another proposal, at

shareholder proposals which raise the same kinds of micromanagement and substantial implementation arguments that we believe wrongly led to exclusion of important climate change shareholder proposals in recent years.

The importance and urgency of climate change responses requires the rethinking of the applicability of the doctrines to climate change related proposals. We hope you will use the current opportunity to create a climate change agenda for the SEC that includes reconsideration of no-action precedents and staff legal bulletins that interfere with shareholder responses to climate change.

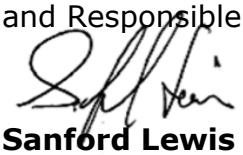
To discuss these matters further, feel free to either contact Sanford Lewis of the Shareholder Rights Group at 413-549-7333 or Jonas Kron, Chief Advocacy Officer of Trillium Asset Management at 503-592-0864.

Respectfully,

Mindy Lubber
Chief Executive Officer and President
Ceres

Josh Zinner
Chief Executive Officer
Interfaith Center on Corporate Responsibility

Lisa Woll
Chief Executive Officer
US SIF: The Forum for Sustainable and Responsible Investment



Sanford Lewis
Director
Shareholder Rights Group

ExxonMobil, asks the company to prepare an audited report on how the IEA net zero scenario would alter the results reported in the company's financial statements. In each instance, the companies' no-action requests assert both micromanagement and substantial implementation; both doctrines have suffered distorted interpretations in the last four years that have led to what we believe are inappropriate exclusions on either basis. Inevitably, there will be other similar challenges as the no-action season continues.

Shareholder Rights Group

Briefing Paper for Biden Transition: Securities Regulation Agency Review Team on Shareholder Proposal Guidance and Decisions at Securities and Exchange Commission

SEC staff rulings of the last four years have systematically undermined shareholder rights, and threatened to disrupt long-standing, productive relationships between investors and companies on environmental and social issues, and between small and large investors on corporate governance. The new administration should reverse the distorted interpretations of micromanagement contained in no-action decisions and should revoke the relevant parts of *Staff Legal Bulletins 141, 14J and 14K.*

Analysis and Recommendations of the
Shareholder Rights Group and
Interfaith Center on Corporate Responsibility

December 15, 2020

Interfaith Center on Corporate Responsibility

About the Interfaith Center on Corporate Responsibility (ICCR) Celebrating its 49th year, ICCR is the pioneer coalition of shareholder advocates who view the management of their investments as a catalyst for social change. Its 300-member organizations comprise faith communities, socially responsible asset managers, unions, pensions, NGOs and other socially responsible investors with combined assets of over $2 trillion. ICCR members engage hundreds of corporations annually in an effort to foster greater corporate accountability.
www.ICCR.org

Shareholder Rights Group

The Shareholder Rights Group is an association of investors defending shareowners' rights to engage with public companies on governance and long-term value creation.
Members of the Shareholder Rights Group include: Arjuna Capital, As You Sow, Boston Common Asset Management, Boston Trust Walden, Clean Yield Asset Management, First Affirmative Financial Network, Harrington Investments, Jantz Management, John Chevedden, Natural Investments, Newground Social Investment, NorthStar Asset Management, Impax Asset Management, Sustainability Group of Loring, Wolcott & Coolidge, Trillium Asset Management.
www.ShareholderRightsGroup.com

About the Author

Sanford Lewis is the Director of the Shareholder Rights Group and an attorney focused on shareholder rights and environmental and social disclosure requirements of the Securities and Exchange Commission. He was co-author of *Fooling Investors and Fooling Themselves: How Aggressive Corporate Accounting and Asset Management Tactics Can Lead to Environmental Accounting Fraud.*

Executive Summary

The incoming administration of President-elect Biden has stated priorities to address the COVID-19 pandemic, economic recovery, racial equity, and climate change. One of the most effective and administratively available mechanisms for addressing all of these issues is for the Securities and Exchange Commission (SEC) to reenable the investors in public companies to file shareholder proposals encouraging improved performance on these issues by their companies.

The right to file proposals to improve corporate performance was cast in doubt by a series of staff level policy changes that occurred at the SEC during the four years of the Trump Administration and with the appointment of William Hinman as the Director of the Division of Corporation Finance. A Staff decision in the incoming administration can correct this erroneous and unlawful reinterpretation of the Shareholder Proposal Rule (Rule 14a-8).

While a promulgated rulemaking has been the most visible change made by the Commission regarding the shareholder proposal process,[1] other sub-regulatory interpretations issued by the Commission's staff under Director Hinman's direction altered the working rules to exclude many long-standing shareholder proposals, placing the shareholder proposal process out of reach for shareholders that want to request better corporate performance on environmental social and governance (ESG) matters by their investee companies.

Prior to Director Hinman's administration, it was well understood by the Staff of the Division of Corporation Finance that one commonplace and appropriate focus of shareholder proposals is to ask companies to redirect their behavior to reduce the company's impact on the environment or society – for instance, proposals commonly have asked companies phase out harmful aspects of their operations (napalm/ nuclear power, etc.), or reduce the amount of greenhouse gases emitted by operations, or to withdraw business operations from developing nations where the company may be implicated in genocide or other human rights atrocities.

Under a series of interpretations issued under Director Hinman, however, shareholder proposals were blocked when they were focused on asking a company to step up the scale and pace of its responses to climate change in alignment with the Paris Agreement, to establish a board committee to address a major shareholder concern, and or to encourage a company to screen its clients to prevent financial support for genocide. In each instance, a new Staff interpretation of micromanagement led to overturning a long record of prior staff support of those proposals.

[1] The rule was revised by the Commission in a controversial 2020 rulemaking (85 Fed. Reg. 70240, Release number 34-89964) which altered the thresholds for filing and resubmission of proposals and included a number of other revisions which undercut the rights of shareholders. Although undoing the damage of that rulemaking is also an important priority. For shareholder proponents, the current briefing paper focuses on an equally damaging set of actions in the prior administration that can be corrected through administrative interpretive action.

The new Hinman era staff position required re-examination of any proposal as to whether the "strategy, method, action, outcome or timeline" was specific.

As such, the Staff's new approach extended a broad "escape hatch" from proposals that might make a specific request for a company to improve its performance in a particular issue area — the opportunity for issuers to challenge any proposal that dares to follow the literal language of the rule which requires that they state "as clearly as possible the course of action that you believe the company should follow."

Background

Rule 14a-8 administered by the Securities and Exchange Commission has long established rules allowing investors to file proposals to be considered by fellow investors through public companies' annual corporate proxy statements.[2] Through the proposal process shareholders raise issues on critical risks, repair dysfunctional corporate governance systems, and provide feedback to their investee companies on the critical issues expected to be significant to those companies in the coming years.

Shareholder proposals are typically non-binding. They offer a flexible mechanism for investors with diverse goals and objectives to request enhanced disclosures and increased accountability of corporate boards and managers regarding emerging, neglected, or systemic long-term risks and opportunities. Many current corporate practices, such as the issuance of sustainability reports and effective attention to long-term environmental and social risks such as climate change, have been substantially initiated and shaped by shareholder proposals.

SEC Rule 14a-8 sets forth the process for determining whether or not a shareholder proposal may appear on a corporation's annual proxy statement. Decision-making under this rule is overseen by SEC Staff ("Staff") through an informal process of correspondence between companies, Staff and proponents. The rule contains over a dozen different grounds on which a proposal can be excluded, including relevance to the company, conflict with state law, duplication of other proposals, personal grievance, vague or misleading, as well as whether the proposal addresses the company's ordinary business. If a company's corporate secretary or general counsel conclude that a proposal violates one of the exclusion criteria articulated in the rule, the company can submit a letter to the Staff requesting a confirmation that the Staff will "take no action" if the Company omits the proposal from the proxy statement. This *no-action letter process* decides the fate of hundreds of company proposals each year.

The Staff interpretations in the no-action process are determinative of whether companies can exclude shareholder proposals from the annual proxy statement under rule 14a-8.[3] Over the course of four years, the Division of Corporation Finance staff under the direction of William

[2] 17 CFR 240.14a-8, https://www.gpo.gov/fdsys/pkg/CFR-2013-title17-vol3/pdf/CFR-2013-title17-vol3-sec240-14a-8.pdf
[3] 17 CFR 240.14a-8, https://www.gpo.gov/fdsys/pkg/CFR-2013-title17-vol3/pdf/CFR-2013-title17-vol3-sec240-14a-8.pdf

Hinman took incremental steps in reinterpreting the ordinary business rule in a number of ways. Most significantly, the Staff decisions led to a much broader definition of when a proposal is excludable because the Staff views the proposal as micromanaging the company. Taken together, the result of the actions in the last four years has been to **impose radical new limitations** preventing shareholders from filing long-standing types of proposals that ask companies to improve environmental, social and governance performance.

We believe correction of these misdirected interpretations merits priority attention from the incoming administration, because the shareholder proposal process, and the private ordering arrangements that it fosters on issues like climate change, executive compensation, product safety, governance, and diversity and inclusion enable investors to simultaneously protect long term value by advancing risk management, while addressing some of our most vexing social issues.

The shareholder proposals that are being stifled by the new interpretation include those that would address the incoming administration's four priority goals of pandemic recovery, economy recovery, racial equity and climate change. Shareholder empowerment and government responsiveness to these four issues go hand-in-hand. While the shareholder proposal process is no substitute for effective regulatory action by agencies like the Environmental Protection Agency, much of the progress in advancement of these issues by the private sector is spurred by the interactions and engagement that the shareholder proposal process enables. The hurdles placed on this process during the Hinman era represent a setback of the momentum on the very issues that are at the top of the agenda for the incoming administration.

At a time in which shareholder proposals are receiving unprecedented levels of voting support due to the recognition of the proposals' insight into investment risks, the Staff's restrictive interpretations of *micromanagement* and *ordinary business* from 2017-2020 threaten to undermine market-wide investment objectives on an array of issues implicating corporate risk management and financial and ESG performance.

The shareholder proposal process implicates issues of long-term value at companies across portfolios and the market in its totality.[4] About a third of assets under professional management in the US ($12 trillion as of 2018) are engaged in sustainable, responsible, or impact investing in the United States.[5] These investors and advisors bear responsibility, through contract and client expectations to ensure that investments are managed consistently with a client's or trustee's strategy/investment mission and, in many cases, a commitment to directly engage with portfolio companies on long-term risks and opportunities.

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[4] The guardrails of the process ensure that the focus of the proposal is of salient interest to investors in the company – both "economically relevant" pursuant to Rule 14a-8(i)(5) and "significant to the company" for purposes of Rule 14a-8(i)(7) and recent Staff Legal Bulletins 14 I, J and K.

[5] US SIF, *Report on US Sustainable, Responsible and Impact Investing Trends 2020*. Worldwide, the assets committed to responsible, long-term investment includes over 1,400 signatories managing more than US$59 trillion that have endorsed the global Principles of Responsible Investment. United Nations Environmental Programme – Financial Initiative, *Principles for Responsible Investment: An investor initiative in partnership with UNEP Finance initiative and the UN Global Compact*, 2016, pp 4.

Moreover, index and passive investors are becoming increasingly aware that they cannot ignore, but rather must be attentive to, the systemic effects of their portfolio investments. For institutional investors, whose diversified portfolios are necessarily spread broadly across the whole economy, there is growing recognition of a fiduciary obligation to consider the prospects both for longer-term performance and systemic impacts, i.e., of the issuing company's effects on the whole economy and environment. This brings heightened attention and sensitivity by the investors to issues of long-term risk, especially "low road" business strategies demonstrating efforts by the corporation to attempt to externalize costs (e.g., pollution of the atmosphere) on the rest of society. In a growing number of instances, even at large investment firms like BlackRock and Vanguard, this leads to support for shareholder proposals addressing long-term ESG issues such as climate change.[6]

Proposals that address a wide range of systemic risks, portfolio-wide risks, and ESG performance are now in the crosshairs of the Staff's "new micromanagement." As one example, consider the impact of climate change across portfolios. As the Mercer report, *Investing in a Time of Climate Change: The Sequel* said:

> "Investors such as pension funds, insurers, wealth managers, and endowments and foundations typically have multidecade time horizons, with portfolio exposure across the global economy. The implications of climate change are systemic and are already apparent … Financial regulators, and particularly for pension funds, are increasingly reinforcing this message by formalizing the expectations that investors should consider the materiality of climate-related risks and manage them accordingly, consistent with their fiduciary duties."[7]

New Staff Position

The new staff position on micromanagement implies that **any proposal which seeks a specific outcome** may potentially be characterized as overstepping board and management discretion. In application to no action decisions regarding shareholder proposals, the new broad interpretation has proven to be an expansive opportunity to curtail shareholder rights.

During the last four years, major categories of proposals that were previously found to be acceptable were swallowed up by this new expansive micromanagement doctrine. Indeed, the new doctrine is so open-ended that it invites and encourages unelected SEC staff to make arbitrary determinations to overturn long-standing precedents. Key areas where this has

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[6] A recent state of the industry report, "Tipping Points 2016" found that financial returns and risk reduction are two primary motivators for a growing portion of capital providers to approach investment decisions on a systemic basis. http://tiiproject.com/tiiping-points-2016 (hereinafter "Tipping Points") The study collected data from a group of 50 institutions, including 28 asset owners and 22 asset managers. The report sought to assess whether and to what extent institutional investors consider and manage their impacts on environmental, societal, and financial systems, and to what extent they consider those systems' impacts on their portfolios.

[7] *Investing in a Time of Climate Change: The Sequel 2019*, Mercer (2019), p. 6.

happened include the ability of shareholders to:

- Ask a company to set greenhouse gas targets aligned with global climate goals;
- Ask a financial services company to screen its client relations for genocide risk;
- Ask a company to establish a special committee of the board;
- File previously permissible proposals regarding executives' golden parachutes.

In each instance, long-standing staff precedents allowed such proposals over companies' ordinary business and micromanagement objections. Yet, applying the Staff's new micromanagement criteria, these critical shareholder proposal models were excluded.

Other Issues

In addition to the radical reinterpretation of micromanagement under the Hinman Division of Corporation Finance, a number of other changes were made which increased costs and uncertainty for proponents and companies. Those additional changes included imposing a new requirement for corporate boards to issue findings regarding shareholder proposals, altering the rules regarding the test for whether a proposal is economically relevant to a company, eliminating the practice of consistently issuing written decisions in response to no action requests, loosening the staff criteria for finding a proposal to be "substantially implemented", and extending ordinary business exclusions to worker health and safety and executive compensation proposals.

Recommendations

We recommend that the incoming administration issue a new Staff Legal Bulletin to:

- Continue to recognize the critical role of investors in advancing both disclosure and action on long term business strategy on ESG matters, including goal setting and increasing the scale, pace and rigor of company responses to significant policy issues.

- Confirm that advisory proposals requesting that a company set targets or improve its performance on significant policy issues are not considered micromanagement unless they attempt to direct minutiae of operations.

- Bring the micromanagement doctrine back into alignment with the Commission's stated policies that "most proposals that are cast as recommendations or requests that the board of directors take specified action are proper under state law," and that shareholders should, in their proposals "state as clearly as possible" the specific action sought under the proposal.

- Rescind the decision of September 6, 2019 to decline to issue written no action decisions, and to resume the process of issuing written determinations in every no action decision.

• Restore prior interpretations and staff precedents in interpretation of ordinary business, relevance and substantial implementation.

The Role of Shareholder Proposals in Addressing Biden Transition Priorities

Shareholder proposals can help to advance many of the incoming administration's priorities

The incoming administration of President-elect Biden has stated priorities to address the COVID-19 pandemic, economic recovery, racial equity, and climate change. One of the most effective and administratively available mechanisms for addressing all of these issues is for the Securities and Exchange Commission (SEC) to reenable the investors in public companies to file shareholder proposals encouraging improved performance on these issues by their companies.

Such efforts of shareholders are crucial to the process and tradition long promoted by the SEC[8] as well as the states in promoting "private ordering" — the process of adjusting social norms by private parties. Private ordering in shareholder proposals has long been involved in promoting issues related to public health, economic progress and equity, racial justice, and climate change. The shareholder proposal process is a pivotal engine for creating such private ordering, because it provides the leverage for shareholders to encourage their companies to reform their governance, enhance disclosure, and reinforce long-term value for investors by reducing a company's impact on society and the environment.

Climate Change

As discussed in depth in this briefing paper, climate change related proposals have helped to move the needle on private sector responses to climate change, especially on disclosure, but recent SEC staff decisions have thwarted core shareholder initiatives seeking the establishment of targets aligned with the Paris Agreement. To cite a couple of examples of climate initiatives driven by investors, Seventh Generation Interfaith (SGI), a coalition of 40 faith-based and values-driven institutional investors located in the Mid-Western United States, have filed shareholder proposals with major impact on midwestern utility companies.[9] A broader market-wide

[8] Many crucial governance reforms that make corporations more efficient and accountable are attributable to this private ordering process. For example, Commission Chair Mary Jo White gave a speech in 2016 describing the prominent examples of market-wide success in private ordering, including the near disappearance of staggered boards, majority vote standards becoming the norm across the S&P 1500, and the recent successes of proxy access proposals resulting in 35% of the S&P 500 adopting proxy access. For each of these examples of private ordering, the shareholder proposal process was a pivotal engine for change. Mary Jo White, Focusing the Lens of Disclosure to Set the Path Forward on Board Diversity, Non-GAAP, and Sustainability, June 27, 2016. https://www.sec.gov/news/speech/chair-white-icgn-speech.html.

[9] Proposals submitted to the WEC Energy Group and CMS Energy Corporation asked each to publish an assessment of the long term impacts on the company's portfolio of public policies and technological advances consistent with limiting global warming to no more than two degrees Celsius over pre-industrial levels. The proposals were withdrawn upon company commitments and subsequent publishing of scenario analyses, and leading to aggressive GHG reduction goals. (See CMS Energy Climate Assessment Report; WEC Pathway to a Cleaner Energy Future). Engagement with Xcel Energy preceded a groundbreaking announcement of the company's commitment to zero-carbon electricity by 2050 and publishing of their Carbon Report (Xcel

initiative, the Climate Action 100+ (CA 100+) initiative, a coalition of more than 500 investors with over $47 trillion in assets, issued a Net Zero Company Benchmark (Benchmark) outlining metrics that create climate accountability for companies and transparency and comparability for shareholders on greenhouse gas (GHG) emissions, improved climate governance, and climate related financial disclosures. Among other things, the CA 100+ advances proposals encouraging companies to set GHG targets. Notably, support for shareholder proposals on climate change is coming from a wide swath of the investing marketplace, with market giant BlackRock recently announcing its forthcoming support of more shareholder proposals on climate change.[10]

Economic Recovery

One stated priority for the Biden transition is the all-important U.S. economic recovery. President-elect Biden has stated a clear directive that we should "build back better," and the work of shareholders in engaging with their investee companies is one of the strongest vehicles for helping to make that happen. Analysts have determined that *resilient* companies have fared better through the pandemic, and are best poised to bounce back. It turns out that resilient companies are typically the most attentive to many material issues of environment, social and governance issues.

Julie Gorte of Impax Asset Management documents the close linkage between ESG related shareholder proposals and the resilient companies that are doing the best during economic recovery:

> As the SEC notes, investors — both bondholders and equity holders — are likely to lose substantial value when companies in their portfolios declare bankruptcy, even if they emerge from it later….. environmental, social and governance factors (ESG) are related to bankruptcies; a report from Bank of America Merrill Lynch noted that of the 17 S&P 500 companies that went bankrupt between 2005 and 2015, 15 scored poorly on ESG scores five years before the event.
>
> Bankruptcy isn't the only indicator of poor management decision-making. There are countless additional examples of poor corporate decision-making that resulted in loss of shareholder value. Some high-profile examples include Wells Fargo's manipulation of customer accounts, BP's poor safety record, which contributed to the Deepwater Horizon blowout, and Volkswagen's emissions cheating scheme. Bank of America researchers found that controversies can be costly: Companies in the Russell 3000 Index with lower controversy scores consistently outperformed those with rising controversies between 2007 and 2020, and ESG controversies were a particularly useful way to identify higher-risk companies.

Energy Building a Carbon-free Future). A proposal at MGE Energy, subsequently withdrawn, also led to their announced commitment to net-zero carbon electricity (Wisconsin State Journal, May 14, 2019).

[10] https://www.ft.com/content/d47a23bb-5c50-4aa6-adde-de0113395827?shareType=nongift

> To be fair, asset managers — at least, active managers — own company stocks because they believe that the companies offer value to the portfolio, and often this is because management has made a great many correct, value-adding decisions. What we don't own, though, is perfect companies. We don't even know of any. We don't always presume management is right, and the proxy vote is one of the few reliable means we have to let management know our judgments on strategic decisions involving corporate value.[11]

Racial equity

As the murder of George Floyd and other documented incidents of police brutality against Black communities catalyzed the unprecedented Black Lives Matter protests, public, company and investor focus on issues of racial justice has increased. These concerns elevated the importance of an array of ongoing shareholder initiatives seeking to address discrimination and harassment, diversity and inclusion, civil and human rights, and social equity. Long-standing shareholder proposals have scrutinized predatory lending, worker health and safety, board and workforce diversity, racial biases in facial recognition software, prison labor, and gender and racial pay gaps.

Many proposals suggested companies set timebound benchmarks to increase diversity. Aflac shareholders argued that "diversity benchmarks can help ensure companies hiring hundreds of financial professionals, such as Aflac Inc., create competitive workforces. Companies that are publicly accountable to diversity goals are most likely to make rapid progress toward achieving their goals." Shareholders of Aflac Inc., Visa Inc., and FifthThird Bancorp, just to name a few, requested diversity reports and timebound benchmarks from their companies to ensure company diversity.

Other proposals have targeted particular problems in different sectors. As one example, both Facebook and Alphabet (parent company of Google) have faced proposals addressing aspects of their civil rights records, with a proposal at Facebook seeking to add high level human and civil rights expertise to the board, and a proposal at Alphabet honing in on the claims of former and current Alphabet employees that they have been fired or reprimanded for whistleblowing on racism, sexism, and other forms of discrimination. A shareholder proposal filed for the 2020 annual meeting asked the Board of Directors to evaluate "the company's whistleblower policies and practices and assessing the feasibility of expanding those policies."

Worker health and safety in the pandemic

During the pandemic the meatpacking sector in particular has been a confluence of the racial justice and COVID-19 crises, with the disproportionately Black, Asian, and Latino workers in the sector being hardest hit by COVID-19. A coalition of 122 organizations wrote to the largest investors of meat-processor Tyson Foods, asserting that "[t]hrough its failure to adequately

[11] Julie Gorte, Ph.D.,The Value of the (Shareholder) Vote: Not Zero, October 29, 2020

protect its workers, Tyson has sent the message that the lives of its workers — who are mostly people of color and immigrants — do not matter to them."[12] A shareholder proposal filed for the 2020 proxy season asked that the Board of Directors to prepare a report on Tyson's human rights due diligence process. The report would go beyond merely diagnosing the problem, to also "prevent and mitigate… human rights impacts." The proposal was written prior to the pandemic, but had highlighted a vulnerability of Tyson, as the pandemic brought to light failures to have effective risk management systems in place that resulted in worker health and safety breaches, and discriminatory impacts of company practices.

The issue of worker health and safety has previously surfaced in many shareholder proposals, including a long-standing proposal regarding implementation of International Labor Organization standards which the Staff found not excludable under the ordinary business rule at *Revlon Inc.* (April 5, 2002).[13] As we will see later in this paper, under recent decisions of the Division of Corporation Finance worker health and safety related proposals have not fared well, but instead have been excluded as ordinary business.

Analysis of Hinman Era Decision-Making Thwarting Shareholder Proposals

SEC Commission Level Articulation of Micromanagement

Ever since the Commission and courts began to allow shareholders to deliberate through the shareholder proposal process on the significant issues facing their companies, conflict has arisen regarding the extent to which shareholders are entitled to deliberate on a company's so-called "ordinary business."

The ordinary business rule, Rule 14a-8(i)(7), from its outset has been intended to ensure that the SEC's administration of shareholder proposals does not overstep managerial and board discretion. A complex set of rules and contingencies have evolved to balance the interests of investors and of the company insiders:

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[12] Wrongful death lawsuit filed by families of 3 Tyson employees: https://www.vbattorneys.com/hubfs/DOC%2001%20-%2005.15.20%20FS%20Original%20Complaint%20.pdf

[13] The proposal requested that the company commit to implementing, through a code of conduct and outside, independent monitoring, the International Labor Organization human rights standards which state that:

1) All workers have the right to form and join trade unions and to bargain collectively. (ILO Conventions 87 and 98)
2) Workers representatives shall not be the subject of discrimination and shall have access to all workplaces necessary to enable them to carry out their representation functions. (ILO Convention 135)
*3) There shall be no discrimination or intimidation in employment. Equality of opportunity and treatment shall be provided regardless of race, color, sex, religion, political opinion, age, nationality, social origin, or other distinguishing characteristics. (ILO Convention 100 and 111)
4) Employment shall be freely chosen. There shall be no use of force, including bonded or prison labor. (ILO Conventions 29 and 105)
5) There shall be no use of child labor. (ILO Convention 138).

• In general, shareholders are not entitled to file proposals addressing the "ordinary business" of a company, which are matters reserved to the board and management.

• An exception is made for "transcendent policy issues," which are those large and widely debated issues facing society that also relate significantly to the company or its business. Examples of significant policy issues that have long been considered appropriate topics for shareholder proposals include climate change, board and employee diversity, and human rights impacts of company operations.

• If a proposal's subject matter qualifies as a significant policy issue, the proposal can still be excludable based on the ordinary business exclusion if the way it is written constitutes "micromanagement."

Authoritative statements from SEC Commissioners on micromanagement are few and far between, but a critical clarification of the meaning of the concept came from the full Commission, (rather than the Staff) in the background materials for the Commission's 1998 Release.[14] In discussing its deliberations on ordinary business, the Commission wrote:

> …. in the Proposing Release we explained that one of the considerations in making the ordinary business determination was the degree to which the proposal seeks to micro-manage the company. We cited examples such as where the proposal seeks intricate detail or seeks to impose specific time-frames or to impose specific methods for implementing complex policies. Some commenters thought that the examples cited seemed to imply that all proposals seeking detail, or seeking to promote time-frames or methods, necessarily amount to ordinary business.
>
> **We did not intend such an implication. Timing questions, for instance, could involve significant policy where large differences are at stake, and proposals may seek a reasonable level of detail without running afoul of these considerations.**

The 1998 Release also noted that ordinary business "determinations will be made on a case-by-case basis, taking into account factors such as the nature of the proposal and the circumstances of the company to which it is directed."

Thus, the Commission in 1998 articulated an intent to apply a *rule of reason* regarding micromanagement, in which proposals could contain a *reasonable level of detail.* This was necessary for consistency with Rule 14a-8(a), which informs potential proponents that:

> A shareholder proposal is your recommendation or requirement that the company

[14] Release No. 34-40018, May 26, 1998. In the Release, the shareholder proposal rules were put into their plain language Q&A format.

> and/or its board of directors take action, which you intend to present at a meeting of the company's shareholders. Your proposal should state as clearly as possible the course of action that you believe the company should follow. Rule 14a-8(a).

Thus, historically, shareholder proposals that include reasonable detail about the course of action sought from a company have always been encouraged and permissible.[15] This approach of allowing *specific requests* to companies on large strategic corporate matters was reinforced in by Ruth Bader Ginsburg in her appellate court decision in *Roosevelt V E. I. Du Pont de Nemours & Company* (US CA DC) 958 F.2d 416. The case involved a shareholder proposal filed with DuPont seeking a phaseout of ozone-depleting CFCs. Where the company had effectively come into line with the proponent's original requested phaseout date for CFCs, the court held that the negligible difference from the proponent's requested date and the company's planned phaseout date could be considered a matter of ordinary business. *Roosevelt v. E.I. Du Pont De Nemours & Company*, 958 F.2d 416 (1992) ("Dupont").

> Timing questions no doubt reflect "significant policy" when large differences are at stake. That would be the case, for example, if Du Pont projected a phase-out period extending into the new century. On the other hand, were Roosevelt seeking to move up Du Pont's target date by barely a season, the matter would appear much more of an "ordinary" than an extraordinary business judgment…. (*i.e.,* one involving "fundamental business strategy" or "long-term goals). *Roosevelt* at 427

In the decades that followed, numerous proposals on diverse subject matters have appropriately asked companies to alter their business model to reduce large potential impacts on society or the environment, and were not excludable under the ordinary business or micromanagement rules.

It is a bedrock principle of corporate law that the board and management of a company are charged with running the company and must be given sufficient discretion to make decisions necessary to the day to day operation of the company.

To what degree can shareholders weigh in?

The question of whether a shareholder request is considered micromanagement or general ordinary business relates to whether a proposal oversteps the board and management's discretion by attempting to tie management's hands on issues that should be reserved solely to their judgment.

Because most proposals are only advisory in nature and do not bind action of the company even if they receive a majority vote, it has always been well-understood that a shareholder proposal that requests a form of company action does not overstep discretion of board and

[15] In fact, a separate line of SEC decisions under Rule 14a-8(i)(3) have treated proposals as impermissible when the language of the request was too nonspecific (treated as impermissibly vague).

management. They are simply not bound to implement any shareholder recommendation, although the proposal process may cause them to take investor perspectives under advisement.

This understanding was made clear beginning with the 1976 Release regarding the shareholder proposal rule, where the Commission clarified that any proposal that ***required*** an outcome would be scrutinized closely for the potential to conflict with state law that reserves the discretion and operation of the company to the board and management. Therefore, the Commission established in the Note to Rule 14a-8(i)(1),[16] that:

> Depending on the subject matter, some proposals are not considered proper under state law if they would be binding on the company if approved by shareholders**. <u>In our experience, most proposals that are cast as recommendations or requests that the board of directors take specified action are proper under state law.</u>** Accordingly, we will assume that a proposal drafted as a recommendation or suggestion is proper unless the company demonstrates otherwise. [emphasis added]

The underlying rationale of this limitation in the note expressed in the 1976 Release was specifically the *preservation of the discretion of the Board of Directors to act*. The Commission explained:

> … it is the Commission's understanding that the laws of most states do not, for the most part, explicitly indicate those matters which are proper for security holders to act upon but instead provide only that the business and affairs of every corporation organized under this law shall be managed by its board of directors, or words to that effect. Under such a statute, the board may be considered to have exclusive discretion in corporate matters, absent a specific provision to the contrary in the statute itself, or the corporations charter or bylaws. Accordingly, proposals by security holders that mandate or direct the board to take certain action may constitute an unlawful intrusion on the board's discretionary authority under the typical statute. On the other hand, however, **proposals that merely recommend or request that the board take certain action would not appear to be contrary to the typical state statute, since such proposals are merely advisory in nature and would not be binding on the board even if adopted by a majority of the security holders**.

In light of this 1976 determination to interpret proposals with requests for specified action as advisory proposals, the concept of micromanagement evolved to address an issue *other than* interference with board and management discretion – the undesirable potential for a shareholder proposal to address an issue that is either trivial for the company, or that seeks a shareholder vote on an excessively detailed set of guidelines (the equivalent of regulations) that are outside of the shareholders' expertise.

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[16] The rule allows exclusion of proposals which are "Improper under state law: If the proposal is not a proper subject for action by shareholders under the laws of the jurisdiction of the company."

Congruent with the understanding that most proposals do not interfere with board and management discretion if they are stated as recommendations, micromanagement exclusions have focused on detailed prescriptive content or instances where a proposal or otherwise delved too deeply into "the weeds" of day-to-day operations.

An overly prescriptive proposal has the effect of shareholders attempting to impose a regulation on the company's management. Thus historic examples of proposals excluded based on micromanagement have included where a hotel chain was being requested to install low-flow shower heads, and where an energy corporation was asked to limit nitrogen oxide 2.15 pounds of nitrogen oxide per million BTUs.[17] In contrast, proposals that have requested large but specific outcomes related to a significant policy issue, whether that request is the elimination of production of napalm by Dow Chemical during the Vietnam War,[18] or phasing out nuclear power by electric companies,[19] or reducing any company's greenhouse gas emissions[20] have historically **not been seen as micromanaging** unless they became unnecessarily prescriptive.

This was the case, and drafting of proposals advancing investor interests in improved corporate social and environmental performance was a predictable matter, until the Division of Corporation Finance under the direction of William Hinman, made radical incursions on the rights of shareholders to file proposals under the auspices of reinterpreting "micromanagement." The broadest new articulation of micromanagement was contained in the Staff Legal Bulletin 14 K – a radical change in interpretation of the predictable rule laid down by decades of precedent, to open a broad swath of potential corporate arguments that a proposal micromanages by phrasing a request too clearly, in deciding whether to exclude a proposal on the basis of micromanagement, asking:

> whether the proposal… imposes a **specific strategy, method, action, outcome or timeline** for addressing an issue, thereby supplanting the judgment of management and the board.[21]

In dropping this broad new principle into the mix, encouraging Staff to examine a proposal on whether the "strategy, method, action, outcome or timeline" was specific, the bulletin extended a broad "escape hatch" from proposals that might make a specific request for a company to improve its performance in a particular issue area — the opportunity for issuers to challenge

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[17] *Marriott International Inc.* (March 17, 2010) where the proposal addressed minutiae of operations – prescribing the flow limits on showerheads; *Duke Energy Corporation* (February 16, 2001) where the proposal attempted to set what were essentially regulatory limits on the company – an 80% reduction in nitrogen oxide emissions from the company's coal-fired plant and a limit of 0.15 lbs. of nitrogen oxide per million British Thermal Units of heat input for each boiler; *Ford Motor Company*, (March 2, 2004) a *highly detailed study* on global warming. These are important examples of proposals that sought "excess" detail.

[18] *Medical Committee for Human Rights v. SEC,* 432 F.2d 659 (D.C. Cir. 1985)

[19] For instance, the Commission made this clear in the 1976 release:

[A] proposal that a utility company not construct a proposed nuclear power plant has in the past been considered excludable … In retrospect, however, it seems apparent that the economic and safety considerations attendant to nuclear power plants are of such magnitude that a determination whether to construct one is not an "ordinary" business matter. Accordingly, proposals of that nature, as well as others that have major implications, will in the future be considered beyond the realm of an issuer's ordinary business operations, and future interpretative letters of the Commission's staff will reflect that view. (Exchange Act Release 3412999 (Nov. 22, 1976)).

[20] See discussion of greenhouse gas proposals, below.

[21] Staff Legal Bulletin 14 K Oct. 19, 2019.

any proposal that dares to follow the literal language of the rule which requires that they state "as clearly as possible the course of action that you believe the company should follow."

This new staff position implies that **any proposal which seeks a specific outcome** may potentially be characterized as overstepping board and management discretion. In application to no action decisions regarding shareholder proposals, the new broad interpretation has proven to be an expansive opportunity to curtail shareholder rights. During the last four years, major categories of proposals that were previously found to be acceptable were swallowed up by this new expansive micromanagement doctrine. Indeed, the new doctrine is so open-ended that it invites and encourages unelected SEC staff to make arbitrary determinations to overturn long-standing precedents. Three key areas where this has happened include the ability of shareholders to:

- Ask a company to set greenhouse gas targets aligned with global climate goals;
- Ask a financial services company to screen its client relations for genocide risk;
- Ask a company to establish a special committee of the board;
- File previously permissible proposals regarding executives' golden parachutes.

In each instance, long-standing staff precedents allowed such proposals over companies' ordinary business and micromanagement objections. Yet, applying the Staff's new micromanagement criteria, these critical shareholder proposal models were excluded.

"Precedent plays an important role in promoting stability and evenhandedness."
John Roberts

EOG Resources: Disposing of "Reasonable Details" Criterion for Micromanagement

The rule of reason was thrown out the window when the Staff made a leap to expand the doctrine of micromanagement — and beyond the Commission's prior policy directives – in *EOG Resources* (Feb. 26, 2018). Contrary to prior proposals that arguably were overly prescriptive in detail, the EOG proposal avoided intricate detail:

> Shareholders request EOG Resources, Inc. (EOG) adopt company-wide, quantitative, time bound targets for reducing greenhouse gas (GHG) emissions and issue a report, at reasonable cost and omitting proprietary information, discussing its plans and progress towards achieving these targets.

The Proposal was a strategic, big picture request framed with minimal details and methods. The Proposal's request to describe medium- and long-term goals for GHG reduction represents a key strategy among investors to assess whether a firm's scale and pace of activity in response to climate change is in alignment with their understanding of transition risks and global and public expectations. **The Proposal addressed a significant policy issue for the Company, included only *reasonable details and methods, and therefore the expectation of the shareholders was, based on prior Staff precedents, that the proposal did not micromanage. Apparently, however, the staff was now treating as micromanagement the simple request to ask the company to set some "Companywide, quantitative, time bound targets."*[22]**

Proposals asking a company to set targets had long been an acceptable and appropriate method for achieving important public policy goals. For instance, in *Exxon Mobil Corp.* (March 23, 2007) a proposal asking the board to "adopt quantitative goals, based on current technologies, for reducing total GHG emissions from the Company's products and operations; and that the Company report to shareholders by September 30, 2007, on its plans to achieve these goals" was found not excludable under Rule 14a-8(i)(7), despite the Company's claim of micromanagement. In *Exxon Mobil Corporation* (March 12, 2007) the proposal requested that the board adopt a policy of significantly increasing renewable energy sourcing globally, with recommended goals in the range of between 15%-25% of its energy sourcing by between 2015-2025. Again, the Staff declined to treat this "method" as micromanagement under Rule 14a-

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[22] In seeking reconsideration of the EOG decision, the proponent Trillium Asset Management wrote:

> It is impossible to overstate both the scope of the shareholder activity and interest in this issue that could be halted if the EOG no-action letter exemplifies a new interpretation of micromanagement. For over 15 years, shareholders have filed shareholder proposals at a wide variety of companies asking them to set quantitative, time-bound greenhouse gas emissions reduction goals. As a consequence, the EOG no-action letter can be seen by shareholders as a potentially dramatic interference with the marketplace. According to Institutional Shareholder Services records of shareholder proposals filed at the Russell 3000 since 2004, shareholders have filed over 150 shareholder proposals asking companies to set greenhouse gas emissions goals. From 2004 -- 2017 these proposals received a median vote of 26%. And in the 2016-2017 time period the median vote was 31.9%. At EOG, a similar proposal, which focused on methane[1] reduction goals, was voted on in 2014 and 2015 receiving votes of 28% and 31% respectively. Clearly these are proposals that investors, including EOG shareholders, are quite familiar with and comfortable forming opinions upon.
>
> While these proposals are filed at companies in many different industries and sectors, these GHG emission reduction goal proposals are often filed at oil and gas companies like EOG: Chevron Corporation -- 2016, 2015; Marathon Petroleum Corporation -- 2016, 2015, 2014; Exxon Mobil Corporation -- 2015, 2014, 2013, 2012, 2011; Phillips 66 Co. -- 2015, 2014
> Valero Energy Corporation -- 2015, 2014; ConocoPhillips Co. -- 2014, 2013, 2012, 2011; HollyFrontier Corporation -- 2014
> WPX Energy, Inc. – 2014.
>
> These efforts have contributed to numerous companies setting GHG reduction targets. Over 350 global businesses have committed to setting GHG emissions reduction targets consistent with the global 2-degree temperature rise goal set in the Paris Accords. Over half of EOG's peers in the S&P 500 have set GHG reduction goals. The oil and gas sector is not exempt from this broad movement to set GHG targets. Hess, Apache, Kinder Morgan, and Southwestern Energy are among EOG's peers in the U.S. Oil and Gas sector that have set quantitative, time-bound GHG and/or methane reduction goals. The 10 major international oil and gas companies that constitute the Oil and Gas Climate Initiative, including Shell and BP, recently announced their intention to work towards near-zero methane emissions.
>
> This uptake of target setting by so many companies should be no surprise given the compelling arguments in favor of doing so. Setting GHG reduction targets is frequently found to be a sound business strategy. A 2013 report by CDP, WWF, and McKinsey & Company found that companies with GHG reduction targets achieved 9% better return on invested capital than companies without targets.

8(i)(7).

The *EOG Resources* decision was particular notable because the Staff had previously ruled against exclusion of identical proposals in a number of preceding no-action letters.[23]

The ability of shareholders to ask companies to set targets and to improve performance has been reinforced in proposals addressing many other topics. To cite one example, in *Tyson Foods Inc.* (reconsideration granted Dec. 15, 2009) the proposal was found not to interfere with ordinary business or micromanage in requesting that the board adopt a policy to phase out certain antibiotics and practices for both Tyson's own hog production and (except when precluded by existing contracts) its contract suppliers of hogs.[24]

Rupture of SEC Principles in EOG Resources Decision Affects Other Shareholder Proposals

The new micromanagement principle established in the EOG Resources determination was later extended to several other climate change shareholder proposals,[25]

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[23] Nearly identical proposals had previously been found not excludable despite objections based on micromanagement and ordinary business. For instance, in *ONEOK, Inc.* (February 25, 2008) the proposal requested that the board prepare a report concerning the feasibility of adopting quantitative goals, based on current and emerging technologies, for reducing total greenhouse gas emissions from the company's operations. The company argued the proposal related to the Company's ordinary business operations, adding that ordinary business problems should be confined to management and the board of directors, "since it is it is impracticable for shareholders to decide how to solve such problems at an annual shareholder meeting." However, despite the complexities of the natural gas business, the Staff had rejected the ordinary business and micromanagement arguments.

The same outcome was applied to other companies and sectors. In *Great Plains Energy Incorporated* (February 5, 2015) the proposal directed toward a utility requested that the company adopt quantitative, time bound, carbon dioxide reduction goals to reduce corporate carbon emissions, and issue a report to shareholders on its plans to achieve the carbon reduction goals it sets. As with ONEOK, Great Plains asserted (erroneously) that the proposal:

> …. would mandate a reduction in the proportion of the Company's power that is generated by natural gas and coal. This will necessarily interfere with the Company's ability to make a prudent selection among its alternatives for electricity generation. These decisions are properly left to management, which is capable of acting responsively to shifts in market pricing and demand, as well as longer-term regulatory and legal developments, on behalf of all the Company's stakeholders.

In fact, as an advisory proposal, the proposal did not and could not constrain the discretion of the management to ultimately decide on any change in proportion of natural gas or coal. In rejecting exclusion and following the ONEOK precedent, the Staff *explicitly stated* that the proposal did not micromanage: "In our view, the proposal focuses on reducing greenhouse gas emissions and does not seek to micromanage the company to such a degree that exclusion of the proposal would be appropriate."

[24] The proposal called on the Company to: (1) phase out routine use of animal feeds containing antibiotics that belong to the same classes of drugs administered to humans, except for cases where a treatable bacterial illness has been identified in a herd or group of animals; and (2) implement animal raising practices that do not require routine administration of antibiotics to prevent and control disease, and where this is not feasible, use only antibiotics unrelated to those used in human medicine; and (3) that the Board report to shareowners, at reasonable cost and omitting proprietary information, on the timetable and measures for implementing this policy and annually publish data on types and quantities of antibiotics in the feed given to livestock owned by or purchased by Tyson. (emphasis added)

[25] *MGE Energy Inc.* (March 13, 2019), *PayPal Holdings Inc.* (March 6, 2018), *Wells Fargo and Company* (March 5, 2019), *Devon Energy Corporation* (reconsideration denied ,April 1, 2019) *Exxon Mobil Corporation* (April 2, 2019), *JB Hunt Transport Services* (February 14, 2019), and *Goldman Sachs Group* (March 12, 2019), among others.

Naturally, the new broad articulation of micromanagement also led, beyond EOG Resources, to company no-action requests seeking to extend the damaging new principle to proposals on various other topics such as the use of antibiotics in the supply chain, promotion of gender equity, management of the firm's pollution impacts, impacts on civil rights, and more.

The new "micromanagement" constraint on shareholder proposals are incongruent with decades of experience in the shareholder proposal process, in which a core element of the shareholder proposal process is the opportunity to track and improve a company's strategy for addressing various impacts on society. Proposals directed toward guiding and even redirecting large business strategy decisions on significant policy issues have long been at the core of the shareholder proposal process, and not a basis for exclusion.

The claims that exclusion is appropriate because existing processes are complex, decisions and strategies are well-considered, and priorities have been set, *amounts to an assertion that the performance and goals that the company has adopted reflect the management and board's strategy*, and not subject to intervention by the Company's investors. If this were the case, it would eliminate many if not most shareholder proposals directed toward improving performance or reducing impact of companies. The open-ended rule has thrown into question whether shareholders can still file many of their most successful proposal models.

Overturning staff decisions on company affiliation with genocide

Proposals that seek to discourage company involvement in financing genocide have long been permissible under Staff rulings but were disrupted by the new micromanagement principle. The shareholder proposal process has been critical to shareholder initiatives to persuade their companies not to directly or indirectly support genocide and other human rights abuses in the supply chain. An important reversal of prior staff decisions relating to genocide and human rights occurred in *J.P. Morgan Chase & Co.* (March 13, 2019), excluding a proposal directed toward genocide prevention, overturned many Staff precedents based on ordinary business that previously allowed proposals to ask essentially the same question but came to the opposite result. Numerous past decisions regarding these proposals on investment and genocide, considering the same proposal model that this proposal had followed, did not address ordinary business or micromanage and allowed the proposals to go forward.[26]

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[26] In *J.P. Morgan Chase & Co.* (March 29, 2018), at the same company, the Staff *disallowed* exclusion of a proposal requesting that the board report to shareholders an analysis of how the Company's published corporate values align with its policies regarding investments in companies tied to genocide or crimes against humanity, and specifically explain how its investments in CNPC/PetroChina are consistent with its published corporate values. The Staff ruled against exclusion under rule 14a-8(i)(7). In *ING Emerging Countries Fund* (May 7, 2012), the Staff disallowed exclusion of a proposal requesting that the Board of Trustees of the Fund institute procedures to prevent holding investments in companies that, in the judgment of the Board, substantially contribute to genocide or crimes against humanity, the most egregious violations of human rights. The Staff ruled against exclusion under rule 14a-8(i)(7). In *Certain Fidelity Funds* (January 22, 2008), the Staff disallowed exclusion of a proposal that the Fund's Board institute oversight procedures to screen out investments in companies that, in the judgment of the

Blocking proposal to establish board committee

In the later years of the Hinman implementation, the Staff overturned decades of precedents allowing shareholders to propose that the Board of Directors of the company create a special purpose committee to address an issue of concern to investors.

In 2019 the proposal found not excludable in *Exxon Mobil Corporation* (Seitchik, April 2, 2019) is one example of proposal was found *not* excludable in response to a company argument claiming substantial implementation in requesting the creation of a board committee on climate change to evaluate Exxon Mobil's strategic vision and responses to climate change and to better inform Board decision-making on climate issues. The charter would explicitly require the committee to engage in formal review and oversight of corporate strategy, above and beyond matters of legal compliance, to assess the company's responses to climate related risks and opportunities, including the potential impacts of climate change on business, strategy, financial planning, and the environment.

In advocacy for the proposal, the proponent asserted that the request for a board climate committee represented an important opportunity for shareholders to demand greater board accountability on the issue. Establishing such a board committee and placing members on it gives those board members specific responsibility and focus. By giving the responsibility for a report or policy to a committee, it increases the degree to which members on the committee have the topic and policy within the scope of their fiduciary liability in the event of breach of duties of loyalty, care or impartiality.

But in 2020 when a similar proposal was refiled by the proponent, the company drew upon the Staff's new interpretation of micromanagement to argue that the proposal micromanaged, and the Staff agreed and allowed exclusion. *Exxon Mobil Corporation* (March 6, 2020). The Staff decision stated:

> The Proposal requests that the board charter a new board committee on climate risk to evaluate the board and management's climate strategy and to better inform board decision making on climate risks and opportunities…. **In our view, the Proposal micromanages the Company by dictating that the board charter a new board committee on climate risk. As a result, the Proposal unduly limits the board's flexibility and discretion in determining how the board should oversee climate risk**. Accordingly, we will not recommend enforcement action to the Commission if the Company omits the Proposal from its proxy materials in

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Board, substantially contribute to genocide, patterns of extraordinary and egregious violations of human rights, or crimes against humanity. The Staff ruled against exclusion under rule 14a-8(i)(7). In *Franklin Resources Inc.* (December 30, 2013), the Staff disallowed exclusion of a proposal that the board institute transparent procedures to prevent holding or recommending investments in companies that, in management's judgment, substantially contribute to genocide or crimes against humanity, the most egregious violations of human rights. The Staff ruled against exclusion under rule 14a-8(i)(7), stating, "In our view, the proposal focuses on the significant policy issue of human rights and does not seek to micromanage the company to such a degree that exclusion of the proposal would be appropriate."

reliance on rule 14a-8(i)(7).[27]

An advisory proposal asking the board to establish a committee and delineating some of the issues that such a committee should take up has never been seen as micromanagement before. Long-standing staff precedents rejected an ordinary business or micromanagement assertion.[28]

Hinman Era: Other Interpretations Contradict Commission Rules and Precedents

Under Director William Hinman, the Division of Corporation Finance made a series of Staff interpretive changes which reduced the ability of shareholders to file performance-oriented proposals with assurance that the proposal model was not excludable. Staff interpretive bulletins and no-action decisions advanced new ideas, encouraging companies to submit new arguments to Staff that would overturn long-standing models and precedents, excluding many proposals that were previously non-excludable. The micromanagement decisions discussed above in this paper are only one of the problematic actions taken under the Hinman administration. Below we look at a series of other problematic actions meriting reversal in the new administration.

Board Findings

On November 1, 2017 the SEC issued Staff Legal Bulletin 14I (SLB 14I), inviting boards of directors to submit their findings regarding whether a policy issue raised by a proposal is "significant" to the company under Rule 14a-8(i)(7) and economically relevant under Rule 14a-8(i)(5). This new Staff Legal Bulletin raised concern among investors regarding the potential for

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[27] Examining the language of the proposal in question, it is clear that it did not dictate outcomes of company policy beyond the proposed committee's focus -- that the "charter should explicitly require the committee to report to the full board on corporate strategy, above and beyond matters of legal compliance, assessing the company's responses to climate related risks and opportunities, including the potential impacts of climate change on business, strategy, financial planning, and our company's operating environment." This is not micromanagement; it is clear delineation of a committee's responsibilities. The proposal went on in the supporting statement to describe potential duties and activities that the Board *could* assign or authorize the committee to undertake — that "a board committee *can* conduct a more focused review than the full board, and therefore better inform and strengthen board decision making by issuing reports, engaging with other committees, providing critical analysis and leadership.

[28] In *PepsiCo Inc.* (February 16 , 2012), the proposal requested that the company establish a Risk Oversight Committee of the Board of Directors. The Staff was unable to accept the company's view that this related to ordinary business because the proposal focused on the significant policy issue of the board's role in the oversight of the company's management of risk. In *MasterCard Incorporated* (April 25, 2019), The Proposal requests that the board direct the Nominating and Corporate Governance Committee to create a standing committee to oversee the Company's responses to domestic and international developments in human rights that affect the Company's business. The Staff decision rejected the company's Rule 14a-8(i)(7) arguments, noting that "In our view, the Proposal transcends ordinary business matters." In *Bank of America Corporation* (February 29, 2008), the Staff disallowed exclusion of a proposal that the company amend its bylaws to form a "Board Committee on Human Rights, which is created and authorized to review the implications of company policies, above and beyond matters of legal compliance, for the human rights of individuals in the US and worldwide." The Staff ruled against exclusion under rule 14a-8(i)(7). In *Yahoo! Inc.* (April 16, 2007), the Staff disallowed exclusion of a proposal that sought to amend the bylaws to establish a board committee specifically to review the impact of corporate action on human rights. The Staff ruled against exclusion under rule 14a-8(i)(7). In *American Telephone and Telegraph Company* (January 15, 1981), the Staff disallowed exclusion of a proposal that relates to the appointment of a special committee to evaluate the Company's operation at Sandia Laboratories. The Staff ruled against exclusion under rule 14a-8(c)(7), stating, "It is the Division's view that neither the formation of the committee, nor its proposed duties would be matters relating to the conduct of the ordinary business operations of the Company."

abuse, because it effectively encouraged companies and boards to seek exceptions for companies allowing exclusion of proposals that had previously been found non-excludable. Reviewing the no-action correspondence at the end of the season, it became apparent that the submissions from boards of directors were variable, but it appeared that few outcomes had been changed. In the course of the process, substantial resources were wasted by both proponents and companies revisiting long-standing precedents. In practice, where there has been long-standing acceptance of proposals supported by staff decisions at numerous companies there is and should be a high burden of persuasion on the board to claim an exclusion.

Relevance

In Staff Legal Bulletin No. 14I Staff also announced that it intends to reapply a financial test to items that are "otherwise significantly related" to a company's business. Rule 14a-8(i)(5) permits a company to exclude 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." Previously, a proposal without documented economic impact on a company could nevertheless be "otherwise significantly related to a company" because it raises a fundamental ethical issue was deemed to be relevant regardless of any economic test. But the new Staff position seemed to imply that even a substantial ethical issue for a company might not be enough to deem a proposal relevant. The burden would fall on the proponent to demonstrate a significant effect on the company's business. Despite the importance of an ethical issue to a company, "[t]he mere possibility of reputational or economic harm will not preclude no-action relief." The bulletin demonstrated that the Staff was no longer committed to recognizing long-standing staff principles that have evolved through decades of precedents applicable to relevance, but instead would require some unknown level of documented financial impact in order to survive a relevance challenge under Rule 14a-8(i)(5).

Oral decisions

A September 6, 2019, an "Announcement" of the Division of Corporation Finance[29] regarding Rule 14a-8 no-action requests stated that the Staff would refrain from issuing written no-action decisions in response to each request, but that instead, the range of possible responses to a no-action request from a company would include instances where the Staff "declines to state a view" or responds "orally."

The SEC Staff has for decades made a consistent practice of responding to no-action requests regarding shareholder proposals by either issuing written decisions concurring with the company's legal arguments for exclusion of a proposal, or notifying the company that the

[29] https://www.sec.gov/corpfin/announcement/announcement-rule-14a-8-no-action-requests

Staff is unable to concur. In each instance, the letters that are issued by the Staff state both any section of rule 14a-8 that was determinative in the decision, and a brief one or two sentences explaining the rationale, connecting the law and the facts.[30]

In implementing the new announcement, the Staff opted during the 2019-2020 season to issue **unwritten** decisions in most no-action requests, and limit written decisions to only a small portion of determinations. The decisions are noted in a chart posted to the SEC website. While each of the chart postings notes which rule provisions the staff utilized for its decision, the lack of written published rationales for most decisions has dramatically reduced the amount of searchable information available to the market for proponents and issuers to understand patterns of Staff decisions. In short, this process has resulted in reduced transparency and decreased accountability. The lack of a written record also undermines the ability of the market to gain predictive understanding of Staff thinking, while the lack of transparency prevents legislative oversight.

Substantial implementation and enforced vagueness

The Hinman administration also altered the Staff policies on determining whether or not a proposal has been substantially implemented by a company sufficient for exclusion under Rule 14a-8(i)(10) prior to the Hinman era, the principled approach applied by the Staff required examination of whether a company had implemented the guidelines and essential purpose of a proposal. This was displaced by a more flexible guidance in which it became apparent that, particularly where a report is requested, if a company has published generally on a topic of a proposal, even if it fails to answer the core questions raised by the proposal, the proposal can be deemed to be substantially implemented.

This change in policy works hand-in-hand with the new micromanagement doctrine to have the effect of purging fossil fuel companies' proxy statements from proposals requesting that they reduce their greenhouse gas footprint. As noted above, until the Hinman era's policy drift, it would never have been considered micromanagement to request that a company set medium and long-term GHG reduction goals. The decision in *EOG Resources* discussed above created that new constraint. The Staff did however offer a workaround in Staff Legal Bulletin 14J – the opportunity to frame a proposal's request as a discussion of "benefits and drawbacks" of a

[30] In the past, there were only a few instances in which the Staff declined to issue a decision, typically limited to circumstances in which a pending litigation, or a pending SEC rulemaking or staff deliberation, was focused on interpretation of the Rule 14a-8 exclusion addressed in the no-action request. This process of notifying the parties as to whether or not the Staff would refer a company's exclusion of the proposal for enforcement has generally served the parties well by providing an element of predictability, while the new exceptions to this consistent practice appear to be unbounded by any timeframes or standards of decision. Three exceptional categories where the staff previously declined to make a determination were when the proponent had filed a lawsuit seeking declaratory relief from the courts that a proposal was not excludable, *Gulf Oil Corporation* (February 3, 1982), *Cracker Barrel Old Country Stores, Inc.* (September 21, 1993), during a Rule14a-8 rulemaking in 1983 in which the Commission's interpretation of a number of 14a-8 provisions were in flux , *NL Industries Inc.* (January 27, 1983), and during internal deliberations regarding the applicability of Rule 14a-8(i)(9) in 2015 (E.g. *Apache Corporation* (February 5, 2015).

possible action, or in terms of "if and how" the company could address an issue like aligning with Paris Agreement goals.

Shareholders increasingly talk about the difficulty of "threading the needle" as between micromanagement (proposal being too specific) and substantial implementation (proposal being too vague that even minimal policies are deemed "implementing"). The more equivocal frameworks for advancing proposals, including greenhouse gas reduction proposals at fossil fuel companies ultimately led to the exclusion of the proposals as substantially implemented, whenever the company has published some information that touches even superficially on the topics of interest in the proposal. Climate change proposals drafted in response to the Commission's newly enforced requirement to be nonspecific, to use "if and how" or "benefits and drawbacks" of alignment with the goals of the Paris agreement ultimately led to exclusion of proposals as substantially implemented at *Exxon Mobil Corporation* (April 3, 2019, March 29, 2019), *Hess Corporation* (April 11, 2019). Each of the companies *merely mentioned* the Paris Agreement in their published materials, even though they never answered or analyzed the core questions posed by the proposals, "if and how" the company intended to align its activities with the Paris agreement. Under this new Staff doctrine of substantial implementation, the failure to meet the essential purpose or guidelines of the proposal no longer seemed to be the operative principle.

Ordinary Business

The Commission's general criterion for deciding if a proposal addresses ordinary business is whether it addresses a significant policy issue facing the company. The notion of "significant policy issue" has been informally characterized in staff meetings with stakeholders as focusing on whether a proposal addresses an issue of widespread public debate. Whether or not an issue rises to the level where it is a transcendent issue that overrides ordinary business concerns typically involves individual no action request determinations which ultimately lead to an understanding that particular issues, e.g. climate change" are a significant policy issue – a determination that then carries over efficiently to proposals facing other companies. A fatal flaw in Staff determinations is the failure to recognize a proposal that is *germane* to current debate and public concerns even if it was drafted prior to the emergence of those concerns. A notorious example is the decision at *Amazon.com* (April 1, 2020) asking the board to prepare a report on the steps the Company has taken to reduce the risk of "accidents," including the board's oversight process of safety management, staffing levels, and inspection and maintenance of Company facilities and equipment and those of the Company's dedicated third-party contractors. In defense of the proposal, the proponents had noted how the proposal had become even more relevant to the company in light of the enormous growth and risks associated with the COVID 19 pandemic. The Staff recognized the possible transcendence of the health risks during the pandemic but noted that "the Proposal, which was submitted on December 6, 2019, focuses on workplace accidental injuries." (i.e., the proposal was submitted pre-pandemic).

The Amazon proposal had noted in the supporting statement the high-speed /high stress environment that are at the core of the company's pandemic risk as well as other accidents for the company: "The Company's online retail business provides customers with fast delivery guarantees, including same day service. This creates a high speed, high stress, work environment particularly for employees at the Company's 186 warehouses and drivers of Amazon.com's fleet of 20,000 owned and leased delivery vehicles." The shortsighted exclusion of this proposal based on ordinary business failed both to recognize the significant policy issue associated with all worker health and safety concerns, and to update the Staff position to reflect the extraordinary challenges facing the company and relevance of the proposal to the pandemic, the economic crisis and to investor interests in voting on matters of long-term value impact.

Executive compensation: Inconsistency with Staff precedent

Another area where the Staff has reversed prior ordinary business/micromanagement precedents is in the area of executive compensation. Con Hitchcock, who as an attorney has defended numerous executive compensation related shareholder proposals notes that:

> For many years, executive compensation was a topic viewed as falling comfortably within the definition a company's "ordinary business" affairs, namely, what to pay its executives. That changed in 1990 when the staff reversed itself in the "*Transamerica* letter" and decided that compensation for senior executives would in the future not be viewed as "ordinary business."
>
> That policy change followed a public outcry about outsized "golden parachutes" that companies had adopted for key executives during the takeover battles of the 1980s. Since 1990 the staff allowed shareholders to pursue proposals advocating reforms on a number of dubious practices benefiting senior executives, *e.g.*, backdating option grants so that the options would be in the money, "golden coffin" awards of stock, available only if an executive dies, abuse of perks. These proposals targeted practices that seemed counter to the "pay for performance" philosophy that underlies many corporate compensation practices.
>
> More recently the staff has taken a more restrictive position. In recent years, companies implicated in the opioid crisis routinely excluded their mounting litigation and compliance costs when deciding whether senior executives had "hit their numbers" in terms of achieving target goals. In *Staff Legal Bulletin 14K* (2019) (available at https://www.sec.gov/corpfin/staff-legal-bulletin-14k-shareholder-proposals), the staff said it would view any such proposals as "micromanagement," unless there were carveouts for specific circumstances or the possibility of reasonable exceptions. (That exception, of course, swallows the rule.)
>
> In 2020 the staff agreed with *Republic Services* (2/14/2020) that the company could exclude a proposal asking for a shareholder vote if "golden parachute" awards exceed a

> certain threshold for senior executives who leave a company after a change in control. The staff had approved this garden-variety proposal against ordinary business claims only *the year before* in *Verizon Inc.* (February 15, 2019) .

The new ruling in favor of exclusion was said to be based on micromanagement. As such it exemplifies the manner in which the new concepts of micromanagement were deployed to reverse numerous staff precedents.

Conclusions and Recommendations

The New Administration Can Restore Shareholder Rights

The new micromanagement principles and rulings of the last four years have undermined shareholder rights, and threatened to disrupt long-standing, productive relationships between investors and companies on environmental and social issues, and between small and large investors on corporate governance. The new administration should reverse the distorted interpretations of micromanagement contained in no-action decisions and should revoke the relevant parts of *Staff Legal Bulletins 14I, 14J* and *14K*.

The Staff can revert to the long-standing position on ordinary business previously articulated *in Staff Legal Bulletin 14 E.*

It should be noted that the variability of staff interpretations is a feature of Commission history through which interpretations that have constrained and harmed investors in one administration are rectified in later administrations. An example was the issuance of *Staff Legal Bulletin 14E* in 2009. The Staff Legal Bulletin reflected upon recent Commission experience to note that a rethinking of the interpretation excluding proposals addressing "evaluation of risk" was necessary to avoid harming investors:

> We have recently witnessed a marked increase in the number of no-action requests in which companies seek to exclude proposals as relating to an evaluation of risk. In these requests, companies have frequently argued that proposals that do not explicitly request an evaluation of risk are nonetheless excludable under Rule 14a-8(i)(7) because they would require the company to engage in risk assessment.
>
> Based on our experience in reviewing these requests, we are concerned that our application of the analytical framework discussed in SLB No. 14C may have resulted in the unwarranted exclusion of proposals that relate to the evaluation of risk but that focus on significant policy issues. Indeed, as most corporate decisions involve some evaluation of risk, the evaluation of risk should not be viewed as an end in itself, but rather, as a means to an end. In addition, we have become increasingly cognizant that

the adequacy of risk management and oversight can have major consequences for a company and its shareholders. Accordingly, we have reexamined the analysis that we have used for risk proposals, and upon reexamination, we believe that there is a more appropriate framework to apply for analyzing these proposals.

With its new understanding, the Staff set forth a new guideline for ordinary business determinations in a manner that respected board and management discretion but ensured that proposals that address transcendent policy issues would be acceptable.[31]

Recommendations

• Continue to recognize the critical role of investors in advancing both disclosure and action on long term business strategy on ESG matters, including goal setting and increasing the scale, pace and rigor of company responses to significant policy issues.

• Confirm that advisory proposals requesting that a company set targets or improve its performance on significant policy issues are not considered micromanagement unless they attempt to direct minutiae of operations.

• Bring the micromanagement doctrine back into alignment with the Commission's stated policies that "most proposals that are cast as recommendations or requests that the board of directors take specified action are proper under state law," and that shareholders should, in their proposals "state as clearly as possible" the specific action sought under the proposal.

• Rescind the decision of September 6, 2019 to decline to issue written no action decisions, and to resume the process of issuing written determinations in every no action decision.

• Limit the applicability of "ordinary business" exclusions consistent with Staff Legal Bulletin 14E.

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[31] The Bulletin stated:
On a going-forward basis, rather than focusing on whether a proposal and supporting statement relate to the company engaging in an evaluation of risk, we will instead focus on the subject matter to which the risk pertains or that gives rise to the risk. The fact that a proposal would require an evaluation of risk will not be dispositive of whether the proposal may be excluded under Rule 14a-8(i)(7). Instead, similar to the way in which we analyze proposals asking for the preparation of a report, the formation of a committee or the inclusion of disclosure in a Commission-prescribed document — where we look to the underlying subject matter of the report, committee or disclosure to determine whether the proposal relates to ordinary business — we will consider whether the underlying subject matter of the risk evaluation involves a matter of ordinary business to the company. In those cases in which a proposal's underlying subject matter transcends the day-to-day business matters of the company and raises policy issues so significant that it would be appropriate for a shareholder vote, the proposal generally will not be excludable under Rule 14a-8(i)(7) as long as a sufficient nexus exists between the nature of the proposal and the company. Conversely, in those cases in which a proposal's underlying subject matter involves an ordinary business matter to the company, the proposal generally will be excludable under Rule 14a-8(i)(7). In determining whether the subject matter raises significant policy issues and has a sufficient nexus to the company, as described above, we will apply the same standards that we apply to other types of proposals under Rule 14a-8(i)(7). In addition, we note that there is widespread recognition that the board's role in the oversight of a company's management of risk is a significant policy matter regarding the governance of the corporation. In light of this recognition, a proposal that focuses on the board's role in the oversight of a company's management of risk may transcend the day-to-day business matters of a company and raise policy issues so significant that it would be appropriate for a shareholder vote.

• Restore prior interpretations and staff precedents in interpretation of relevance and substantial implementation.

The shareholder proposal process represents an essential opportunity for shareholders to raise important issues of concern and provide advice to the board and management on strategic management of significant policy issues and long-term value. This important tool should not be denied to shareholders. For the reasons outlined above, the members of the Shareholder Rights Group respectfully submit that these recommendations are prudent and fully aligned with the Commission's mandate to protect and serve investors and the capital markets.

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