NEWS

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AMENDING THE SHAREHOLDER PROPOSAL RULE: A NEW APPROACH

Remarks of
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It is a great pleasure for me to be here today among such vital participants in the American corporate process. I am particularly pleased to have the opportunity to discuss the proposed amendments to the Securities and Exchange Commission's rules governing shareholder proposals, a subject of great and current interest to public companies and their shareholders. This afternoon, I will report to you on where we are, and where we may be going in the shareholder proposal area, and I will leave you with a plan of my own that I believe may present a viable regulatory approach that is more realistic than any of the suggestions to date.

Since 1942, the Commission has provided shareholders of public companies subject to its proxy regulations with a right to have their proposals presented to the issuer's shareholders at large, and to have proxies with respect to such proposals solicited at little or no expense to them. The recognition of such a right reflected the reality that with the increased dispersion of stock ownership in publicly held corporations, the proxy solicitation process, and not the annual meeting itself, had become the real forum for shareholder suffrage.

The right of a shareholder to have his proposals included in a corporation's proxy materials has undergone a number of revisions over the last four decades, with the changes generally directed at refining the bases for exclusion of certain proposals

from the proxy statement. The current rule governing shareholder proposals is provided in Rule 14a-8 under the Securities Exchange Act, which requires, in general, that upon timely submission, an issuer must include a shareholder proposal in its proxy materials, unless it falls within one of thirteen enumerated bases for exclusion. To be eligible to submit a proposal, a shareholder need only own one share of the issuer's stock at the time of submission of the proposal, which he must continue to own through the time of the relevant shareholders meeting. No shareholder may submit more than two proposals per meeting, and neither proposal may exceed 300 words. If an issuer seeks to exclude a proposal, it must notify the Commission and set forth the reasons why it believes it may properly do so. The Commission's Division of Corporation Finance, in turn, must then decide whether or not to issue a no-action letter with respect to the attempted exclusion.

Although this right of virtually unfettered access to the corporate voting process may represent an appropriate ideal, in real-world practice it has, I believe, imposed burdens on both public companies and the Commission staff that are simply not justified. The shareholder resolutions submitted for inclusion in proxy materials all too often may represent self-indulgent attempts to highlight issues of individual significance with little or no real connection to the business of the corporation. The existing bases for

exclusion of proposals contained in the current rule have seemed to many to be inadequate to screen out matters that should have no place on the corporate ballot.

Moreover, shareholders submitting such proposals frequently have little more than a passing interest in the company itself. Indeed, a recent study has indicated that for year-ended June 30, 1982, out of 630 proposals for which information was made available regarding proponent stock ownership, 28 percent (175) were submitted by persons or groups holding less than 10 shares, and 53 percent (332) were submitted by holders of 100 shares or less. In effect, the present system has allowed investors with the barest economic stake in a corporation to turn its proxy statement into a political document and, as often follows, its annual meeting into a personal forum.

The misuse of the proxy system to further personal, and not corporate, aims has other, more tangible costs. First, of course, is the financial impact. Although the expense to an issuer of including a proposal -- typically between $10,000 and $15,000 per proposal -- does not, in most instances, materially impact upon its financial condition, it is nevertheless a cost that is generally unnecessary and is usually unjustified, because shareholder proposals are rarely, if ever, passed, and, generally are of little benefit to the majority of shareholders. In addition, the inclusion in proxy materials of voluminous shareholder proposals tends to undermine the

disclosure value of the entire document, as a typical shareholder may choose not to even open the proxy statement, rather than trying to forge through the protracted text in search of meaningful information.

As I mentioned earlier, the present system also imposes a severe burden on a Commission staff already stretched to its limits by budgetary constraints. In this connection, each time an issuer seeks to exclude a shareholder proposal, it must notify the Commission and seek a "no-action" letter. In fiscal year-ended June 30, 1982 alone, our Division of Corporation Finance responded on 313 occasions to 182 issuers, who contested a total of 487 proposals. What this means in terms of allocation of resources is that the staff spent one entire man-year (1208 hours) in processing materials submitted to it under Rule 14a-8 during the 1982 proxy season.

Against this backdrop, as most of you know, on October 14 of last year, the Commission requested public comment on three separate proposals which would alter, to varying degerees, the existing regulation of the shareholder proposal process.

In brief, the first approach ("Proposal I") would retain the basic framework of the present rule, but would amend certain of its provisions. The most significant changes I believe, would be the inclusion of a requirement that in order to be eligible to submit a proposal, a shareholder would have to have been a record or beneficial owner of at

least one percent, or $1000 in market value, of the issuer's securities entitled to vote at the meeting, for a period of at least one year prior to the meeting. In addition, proponents would only be permitted to submit one proposal for each meeting. Proposal I also provides for other revisions which would broaden certain of the bases for exclusion of proposals already contained in Rule 14a-8.

The second proposal ("Proposal II") offers a much more fundamental change in the shareholder proposal process. Under this plan, the Commission would continue to have a rule that specifies the procedures governing submission and inclusion of shareholder proposals, but would, under a supplemental rule, permit issuers to provide their own guidelines for access to the proxy process, subject to ratification and periodic reapproval, by the shareholders at large. Proposal II would permit issuers to formulate eligibliity requirements and bases for exclusion of proposals more or less restrictive than the Commission's current rule, subject to certain minimum limitations on the eligibility criteria and the bases for exclusion as set by the SEC. For example, the rule might say that no such plan could provide eligibility criteria that would preclude persons holding more than a specified percentage or value of the securities from submitting a proposal.

The third proposal ("Proposal III"), the most radical change from the present scheme, is something of a lottery, and

reflects a view that shareholders should have relatively unimpeded access to the issuer's proxy statement. This lottery approach would require an issuer to include a shareholder proposal as long as it was proper under state law and does not involve the election of directors, subject to a numerical maximum of total proposals per meeting that is keyed to the number of its record shareholders, and does not exceed 12 proposals. If an issuer receives more than the maximum number of proposals required to be included, the proposals are to be divided into two groups -- those submitted by proponents who have had proposals included in the previous three years, and all others proposals. If the number of proposals in the first group exceeds the maximum number, the proposals to be included will be determined by lot. If, on the other hand, the number in the first group is less than the maximum, all such proposals will be included, with the remaining slots filled by lot from proposals in the second group. The lottery rule would be self-generating and would absolve the Commission staff from making a separate determination each time a proposal is sought to be excluded.

To no one's surprise, the public interest in these proposals has been overwhelming, and indeed the response was unprecedented in recent Commission history. Almost 400 letters were received by the staff during the comment period, approximately 300 of which were divided equally among individuals, religious groups, and issuers. The remaining comments came

from institutional investors, law firms, bar associations, and members of both houses of Congress.

Although we have not yet had the opportunity to analyze fully all of the comments, it is quite evident that among those who feel that the present rule needs to be changed, Proposal I was the overwhelming choice. Indeed, less than a dozen of the commentators expressed support for the idea of issuer designed shareholder proposal rules, and virtually no one fa or d the open-access concepts of Proposal III.

If I were required to choose from among the three proposals that I have just described, I believe that Proposal I is the most constructive. It seems neither inequitable nor unrealistic to require some proven economic interest in the issuer before permitting access to its proxy mechanism, and, philosphically I have no problem with an eligibility threshold.

Yet, even that approach raises some concerns. In this connection, I believe it is difficult, and indeed almost arbitrary, to determine precisely where to draw the line of eligibility. In today's economy, a $1000 threshold would probably do little to discourage a corporate gadfly bent on submitting a matter of particular personal concern to an issuer for inclusion in its proxy materials. On the other hand, the $50,000 and $100,000 thresholds suggested in the comments of certain issuers are clearly too high, and may prevent the submission of bona fide proposals from shareholders who have the best interests of the corporation and its shareholders at heart.

I, therefore, would propose a new and simple approach to regulatory reform in this area. My approach would, I believe, keep the door of corporate democracy open to all shareholders while, as a practical matter, discouraging persons seeking a forum but lacking any real investment interest in the issuer from the improper resort to the proxy machinery. My plan is to supplement the existing framework under Rule 14a-8 with an additional provision that would permit issuers to omit the name of the proposing shareholder from proxy materials, even where the proposal and supporting statement are to be included.

Although at first blush, this approach may appear over-simplistic, and, in fact, clearly will not solve all of the current problems in the shareholder proposal process, it seems to me that it may respond directly to the realities of some of the current abuses. My reasoning is based on two fundamental judgments. First, I believe that shareholder proposals represent an important element of the American corporate process, and that the proxy machinery should remain accessible to those shareholders who are legitimately concerned about the business of the company and the well being of all of its shareholders. Second, I am convinced that those who misappropriate the proxy process to air personal or political concerns that have no real nexus to the issuer's business, and are of minimal interest to other shareholders, may do so to reap the rewards of public notoriety. Up until now, some

individuals have found it relatively easy to force the attention of billion dollar businesses and millions of public investors to be focused upon them personally with minimal effort through the shareholder proposal process. Under my new approach, however, the opportunity for personal recognition may be significantly reduced, and, as a result, I believe we might witness a natural decline in the number of political and personal resolutions that have begun to permeate the proxy statement.

The Commission will consider which course to follow sometime this summer.

Conclusion

I have attempted today to outline for you the various approaches we at the SEC are currently considering in our attempt to make the shareholder proposal process a more useful forum for the airing of matters of legitimate business concern to the corporation and its shareholders. I believe that my suggestion to cloak proponents in anonymity might well go a long way towards discouraging the use of the proxy process by self-interested protesters in search of a soapbox, without dismantling the existing system of shareholder access. Although no approach is ironclad, and I am not yet prepared to say that my idea will eliminate all of the abuses we have observed over the years, I do believe that in our imperfect world, removing the recognition factor may be the best possible course to follow.