2023 Proxy Season in Review

August 1, 2023

This past year was the first full proxy season following the effectiveness of Rule 14a-19 under the Securities Exchange Act of 1934, which requires the use of universal proxy cards in contested director elections. Based on the experience of our public company clients, as well as data provided by FactSet and Deal Point Data, we have evaluated some of the predictions made about the universal proxy regime and have tried to identify some initial indicators as to how proxy contests may continue to evolve.

Initial Outcomes of the Universal Proxy Regime

- **Level of Activism**: Many predicted that the universal proxy would increase the number of proxy contests launched, largely because of the expected decrease in cost. However, 2023 saw no material change in the number of proxy contests from the prior year, and in fact the number of contests decreased. During the 2023 proxy season, 13 election contests went to a vote, compared to 17 in the prior period (October through June).

- **Activist Success**: Some predicted that the universal proxy would benefit activists by making it easier to support at least some of their candidates without necessarily committing to the activist's entire slate. The relatively small sample size from the 2023 season probably means it is too early to tell whether the universal proxy has meaningfully tipped the scale in favor of activists. However, the 2023 proxy season saw an increase in the number of outcomes in which the activist won a partial slate, as shown in the chart below.

	Company Wins All	Activist Wins All	Activist Wins Partial
2022	11	5	1
2023	6	3	4

- **Costs of an Activism Campaign**: It was generally predicted that the use of the universal proxy would decrease the costs of launching a proxy contest, principally because the stockholder's nominees would appear on the Company's proxy card and the stockholder could utilize the internet to deliver proxy materials. In 2023, average spending on activist campaigns did not materially change, and even increased a bit over the prior year. It appears that activist stockholders committed to successful campaigns continue to be willing to spend large sums on proxy solicitation efforts.

- **Scrutiny of Individual Nominees**: Because the universal proxy allows stockholders voting by proxy to choose individual nominees from a menu, instead of having to choose a full slate, some predicted that the universal proxy would result in a greater focus on the strengths and weaknesses of individual nominees. In 2023, this prediction appeared to be borne out: many recommendations made by proxy advisory firms ISS and Glass Lewis this past season noted individual nominee qualifications or qualities, such as the long tenure of certain board members and the relevant experience of an activist stockholder's nominees, including, in one case, citing the need for "fresh, independent points of view" in place of a chair who had been on the board for 18 years, and in another, noting a nominee's "mentality, capital allocation expertise, willingness to challenge management and other directors". This focus on individual qualifications continues a trend that predates adoption of the universal proxy rule, but it appears likely that the universal proxy has played a role in deepening it.

Advance Notice Requirements

The adoption of Rule 14a-19 spurred a wave of amendments to companies' bylaws requiring advance notice of stockholder nominations and proposals. The vast majority of these amendments incorporated language expressly referring to the new rule, requiring nominating stockholders to comply with Rule 14a-19's timing and disclosure requirements as well as the requirements that the nominating stockholder file a compliant proxy statement and agree to solicit at least 67% of the shares entitled to vote. In addition, perhaps anticipating an increase in stockholder activism following the new rule, some public companies adopted bylaw amendments that more extensively reworked their advance notice provisions.

One of the most commonly adopted changes was to require nominating stockholders to disclose any arrangements or relationships with third parties that support their nomination activities. While there have been instances of stockholders attempting to resist such requirements, including by making proposals to require stockholder approval prior to adopting any new disclosure requirements, the Delaware Court of Chancery has

indicated (in *Rosenbaum v. CytoDyn Inc.* (Del. Ch. Oct. 13, 2021)) that requiring the disclosure of agreements or associations supporting the stockholder's nomination activities are not "overtly unreasonable," and that the terms of such requirements "comport with bylaws our courts have characterized as 'commonplace'". As a result, we expect that such disclosure requirements will continue to be adopted by public companies.

In some instances, however, where companies have adopted new disclosure requirements that have a more serious impact on the ability of stockholders to nominate directors, these have resulted in a backlash. One example is the legal challenge brought by Politan Capital Management LP against the board of Masimo Corporation, which, a week after meeting with Politan, adopted bylaw amendments requiring any nominating stockholder to disclose, among other things, the names of all passive limited partners and their and their family members' holdings in any competitors of Masimo or any counterparties to litigation with Masimo. Politan sued, claiming these requirements were impossible for many stockholders to comply with, either because this information was unavailable or because of existing confidentiality obligations. Politan asserted that Masimo directors breached their fiduciary duties by adopting amendments that preemptively blocked stockholders from nominating candidates for election to the board. Masimo eventually settled with Politan, and removed these requirements from its bylaws, meaning that there was no judicial resolution of the matter. However, public opinion appeared to weigh heavily against Masimo: proxy advisory firms ISS and Glass Lewis each issued a recommendation in support of Politan's director slate, each citing Masimo's poor corporate governance or "nuclear option" in response to Politan's campaign as one of the reasons for their support. A large majority of stockholders voted for all of Politan's nominees, replacing all of the incumbent directors on Masimo's slate.

The 2023 proxy season has shown that stockholders and proxy advisory firms have limited tolerance for advance notice requirements that are viewed as impeding or stifling the stockholder election process. In multiple instances this season where ISS or Glass Lewis issued a recommendation in favor of one or more of a stockholder's director nominees, they included reasons such as: "reactionary" changes to corporate governance and board composition; "a history of governance measures that are not consistent with best practices, particularly as it relates to shareholder rights"; and "demonstrat[ing] resistance to shareholder input by not seeking to interview the dissident's nominees and only announcing the governance improvements as the proxy campaign was heating up." Nominating stockholders have also demonstrated a willingness to challenge these board actions in court.

In some cases, the legal challenges brought by stockholders were based not on the substance of the advance notice requirement, but rather on the ways the company used

the requirement to reject a stockholder nomination notice. These challenges have not always been successful for stockholders: two recent decisions by the Delaware Court of Chancery, *CytoDyn* (noted above) and *Jorgl v. AIM ImmunoTech Inc.* (Del. Ch. Oct. 28, 2022), each upheld the company's rejection of a stockholder nomination for failure to comply with the disclosure requirements. In both *CytoDyn* and *AIM Immunotech*, the court reviewed the specific circumstances of the rejection of the nomination, including the timing of the bylaw amendments (in both cases the amendments were adopted "on a clear day" long before any proxy contest was launched or threatened) as well as the nature of the stockholder's non-compliance with the bylaw requirements (in both cases the stockholder failed to disclose material arrangements or agreements with third parties who were financing, or even orchestrating, the nomination). A different outcome may result if the bylaw requirement is adopted in response to a specific looming proxy contest, or where a stockholder nomination notice is in material compliance with bylaw disclosure requirements but was rejected by an incumbent board on the pretext of a minor flaw in the notice. As we described in more detail in our Debrief dated July 11, 2023, the Delaware Supreme Court, in *Coster v. UIP Cos., Inc.* (Del. June 28, 2023), recently clarified that when a stockholder challenges a board action that interferes with a contested election of directors, the board must prove that (i) it reasonably perceived a "real and not pretextual," threat to corporate policy or effectiveness, and (ii) the response was reasonable and "not preclusive or coercive to the stockholder franchise." Notably, the Court stated that a threat perceived by the board "cannot be justified on the grounds that the board knows what is in the best interests of stockholders."

Officer Exculpation

One matter not related to Rule 14a-19, but which many Delaware public companies wrestled with during the 2023 proxy season, was whether to propose charter amendments exculpating officers from monetary liability for breaches of the duty of care, as now permitted under Section 102(b)(7) of the Delaware General Corporation Law. Previously, such exculpation was permitted only for directors. Many companies took a "wait and see" approach, looking to the 2023 results of stockholder votes and proxy advisory firm recommendations on these charter amendments. The results will likely embolden Delaware companies waiting on the sidelines: of the proposals put to a stockholder vote, over 85% were approved by stockholders, with proxy advisory firms supporting the amendments in about the same percentage of cases.

Note, however, that there is a case currently pending before the Delaware Supreme Court regarding whether such an amendment requires a separate stockholder class vote for companies with multiple classes of stock. Public companies with dual-class stock

may wish to wait for a final judicial determination before submitting any such amendment to a stockholder vote, unless approval of the amendment will be sought by separate class votes.

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