Session 502 | Effectively Dealing with Shareholder Activists: Learn from the Trenches

So what’s it really like to be the "tip of the spear" for your company's response to a Carl Icahn’s knock on the door? While shareholder activists-who grab stakes in companies and agitate for significant change-can be a force for creating long-term value, the only certainty is many sleepless nights ahead. With behind-the-scenes insights, the panelists will discuss lessons learned from recent, high-profile activist campaigns and the fallout of transformational change that often follows.

Moderator:
Amy Yeung, Comscore, Inc.

Speakers:
Krishna Veeraraghavan, Sullivan & Cromwell
Don Liu, Target
Jung Choi, Stanley, Black & Decker
Henry Wang, Herbalife
Effectively Dealing with Shareholder Activists: Learn from the Trenches

Amy Yeung, Comscore, Inc.
Krishna Veeraraghavan, Sullivan & Cromwell
Don Liu, Target
Jung Choi, Stanley, Black & Decker
Henry Wang, Herbalife

November 9, 2019
Shareholder Activism Overview
Shareholder Activism Highlights

- Shareholder activism is a prominent, and likely permanent, fixture of the corporate governance landscape
  - An ordinary course issue facing companies in the US and around the world – not a sporadic phenomenon
  - Assets managed by activist hedge funds exceed $100 billion
  - Public companies, even those with high market capitalization, are frequently subject to activist campaigns
  - Institutional investors, which collectively own a large portion of most public companies, often provide activists with support and credibility

- It is important to proactively and preemptively address shareholder activism and be prepared at the board and management level
  - Preparation is part of good governance and enables a company to most effectively respond if/when activist investor appears at the door
  - Preparation dovetails with consistent shareholder engagement, which has become an expectation for public companies
Increasing Shareholder Power: Emerging Corporate Governance Best Practices

• Following corporate scandals of early 2000s (Enron, WorldCom, Parmalat, etc.), sea change in corporate governance landscape

• New U.S. regulations (Sarbanes-Oxley, Dodd-Frank) dramatically changed U.S. corporate boards
  • Boards are majority independent; key committees entirely independent
  • Many companies have a lead independent director and/or separate chairman
  • Boards now meet more frequently – both as a whole and in executive session (without the CEO)
  • Director qualifications face more scrutiny, with boards increasingly considering directors by category (i.e., shareholder/investor friendly; relevant industry, financial or cyber experience; diversity)

• Increased focus on year-round shareholder engagement/outreach
  • Management, Corporate Secretary, Investor Relations attendance at investor conferences
  • Senior management focused on building relationships with both portfolio managers and proxy contacts at top shareholders; board members asked to engage with significant investors

• Other changes have increased shareholder power in the U.S.
  • Board members purchasing shares to show alignment with shareholders
  • Continually improved compensation disclosures and incentive transparency
  • SEC rules enable shareholders to interact with each other more freely
  • Shareholder proposals effective at removing classified boards and other takeover defenses, as well as gaining proxy access and the right to call special meetings and act by written consent.
  • Proxy fights and withhold vote campaigns against directors have increased exponentially
Despite ongoing debate by academics and professionals regarding the “short-termism” of activist investors, shareholder activism continues to be a prominent feature of the corporate landscape.

**Capital Fuels Activist Activity**

- Large amount of capital flowed into activist hedge funds in recent years, resulting in hundreds of funds entering the fray
  - Capital invested in new activist positions in 2018 was up $2.5 billion from 2017
- Success in raising funds, gaining board seats and achieving activist objectives has fueled increased activity
  - Overall, the number of shareholder activism campaigns in the U.S. has remained relatively consistent over the past 5 years
    - In 2018, there was a 5% increase in number of publicly announced campaigns against U.S. issuers from 2017
  - However, activists are achieving higher success rates: for every campaign in 2018, activist hedge funds won .81 board seats
  - Most targeted industries are real estate investment funds, mutual funds, packaged software, integrated oil, major pharmaceuticals
- With more capital and credibility, activists (even those with small positions) have targeted even the largest companies
  - In 2018, 11% of companies targeted by an activist had a market cap over $10 billion (slight decrease from 2017, in line with 2015-16)

**Focus on Unlocking Value**

- M&A (sale or breakup), return of capital and operational activism increasingly common
- Many activists are repeat players with long-term strategies
- “Red flags” that attract activists include significant stock price underperformance, operational challenges relative to peers and earnings misses, perceived potential for better performance
  - Recently, companies that have performed in-line with or better than their peers have also become targets, due to activist hesitation to invest in companies with greater operational risk
Public Activism Trend: Board Membership and M&A Activism

- Board-related activism remains the most common objective of activist campaigns.
- Many campaigns feature multiple objectives, with governance activism used to achieve economic objectives.
- Underlying objectives include M&A actions, balance sheet concerns, business strategies and corporate governance.
- Proxy contests focusing on board-related governance in 2018 were well below the five-year average.

Breakdown of 2018 Activist Objectives

- **Objective of Proxy Contest**
- **Objective of Other Stockholder Campaign**
Activism Escalation of Shareholder Engagement

Activists often follow a standard playbook of escalation tactics; key objective is creating impression of inevitability.

**Overview of Tactics**

- **Private Discussions**
  - Activist engages in private dialogue with management/the board
  - Discussions can avoid further agitation or lead to settlement; if unsuccessful, activist could escalate

- **Media and PR Campaign**
  - Activist discloses its stake and an intention to pursue activism
  - Activist initiates a high-profile public campaign designed to put pressure on the board

- **Proxy Contest**
  - Activist may engage in a proxy contest, seeking to elect slate of directors or force/encourage specific action (shareholder proposal)
  - Activist may initiate litigation to challenge board actions

- **“Hostile Offer”**
  - With some notable exceptions (e.g., Icahn, Elliot, Pershing Square), an activist does not often make an offer for the entire company

**Selected Examples**

- ForestCity FirstEnergy
- DOVER Citi
- ALLERGAN vodafone
- Sempra Energy Altaba
- United Technologies
- SandRidge natus.
- Campbells Supervalu
- SUPERVALU newell brands
- Compware AthenaHealth
- ALLERGAN
Shareholder Activist Playbook: Private Discussions

• Activist may seek to engage in private dialogue with management or the board
  • Private letter or email to CEO or directors outlining thesis
  • Activists sometimes approach an outside director (directly or through an intermediary who may know the director) to “get a read” on the board/situation

• Activist may conduct aggressive “diligence” on the company and its directors and officers
  • Background checks on directors and management (potentially including gathering “dirt”)
  • Outreach to ex-employees via social media (e.g., LinkedIn)
  • Outreach to other large shareholders to take their temperature
  • Use of third-party consulting services to analyze the Company’s business and strategy
Shareholder Activist Playbook: Public Agitation

- Activists may initiate a publicity campaign designed to put pressure on the board
  - Publicity campaigns include publicly disclosing presentations about the Company or letters or “white papers” to the company disclosing certain demands; and/or issuing press releases, establishing websites and using Twitter and other forms of social media expressing certain positions and desired objectives

- An activist may need to file a Schedule 13D disclosing its stake (if >5%) and an intention to pursue activism
  - Activists also successfully using smaller stakes (~1%) and ownership of derivatives to press for change

- Publicity typically attracts like-minded investors/other activist funds — “wolf pack”

- Public disclosure has been less prevalent recently, perhaps as a result of increased company engagement and settlements with activists before the activist campaigns become public

- The SEC has generally not been responsive to issuer complaints that activist publicity campaigns are misleading or include inappropriate personal attacks
Shareholder Activist Playbook: Proxy Contests

- If a company refuses an activist’s demand for one or more board seats, the activist can mount a proxy contest at next annual meeting or by calling a special meeting.

- The activist will initiate the proxy contest by submitting a notification of its director nominee(s) to the company during the time period prescribed by the company’s bylaws:
  - Most companies limit director nominations to a 30-day “window” that is either 60-90 or 90-120 days in advance of the prior year’s annual shareholders meeting.
  - The activist’s nominee notification does not require a public filing, but the activist may choose to publicize the nomination(s).

- Between submission of proxy solicitation material to the SEC and the shareholders meeting, both the activist and company will solicit proxies from shareholders:
  - Proxy solicitations take multiple forms, including individual meetings with large institutional shareholders and ISS, mailings, phone calls and social media posts.
  - SEC Rules governs the content, form and public filing of proxy solicitations.

- The outcome of the contest is likely to depend largely on the votes of a relatively small number of institutional investors and ISS/Glass Lewis recommendations.

- Proxy contests can be expensive, but the activist’s expenses often get reimbursed by the target company if the proxy contest later settles.

- The occurrence of a proxy contest, whether or not the activist gains board seats, may be followed by a CEO change, M&A activity and subsequent proxy contests.
Influence of Institutional Investors

• Assets managed by institutional investors have grown significantly—institutional investors own approximately 84% of S&P 500 companies

• Index funds have grown twice as fast as other asset managers over last decade

• Ownership of many U.S. companies is concentrated in hands of small numbers of institutional investors, e.g. BlackRock, Vanguard, State Street, and Fidelity
  • As of December 2018, Blackrock, Vanguard and State Street collectively owned approximately 19% of all S&P 500 shares

• 91% of institutional investor shares are voted, as compared to 28% retail investor shares

• Traditional institutional investors are displaying increased willingness to directly express their views on governance matters and support activism

• An activist’s success in a campaign depends on receiving institutional investor support
  • Concentrated institutional ownership enables activists to rapidly garner support from other shareholders— and failure to receive institutional support is often outcome determinative
  • Increasing support from traditional institutional investors has further emboldened activists— even activists with much smaller ownership interests, who can represent that they “speak for” much larger ownership stakes
  • Some more traditional institutional investors are willing to pair up with an activist in a particular campaign
Proxy Advisory Firms Still Influential

Although their impact has waned in recent years, proxy advisory firms remain influential. An unfavorable recommendation by ISS or (to a lesser degree) Glass Lewis could affect the outcome of a proxy contest.

In contested elections, proxy advisors consider a number of factors:

**FACTORS CONSIDERED**

- ISS asks two questions:
  1. *Has the dissident demonstrated that change is warranted at the company?*
  2. *If change is warranted, are the dissident nominees more likely to effect that change than the management nominees?*

- ISS considers the following factors, among others:
  - Long-term financial performance of target relative to its industry peers
  - Management’s track record
  - Background to the proxy contest
  - Nominee qualifications and any compensatory arrangements
  - Strategic plan of dissident slate and quality of critique against management
  - Likelihood that the proposed goals and objectives can be achieved (both sides)
  - Stock ownership positions

**OTHER OBSERVATIONS**

- Proxy advisory firms generally favor “new blood”— for at least a few seats.
  - Difficult for a dissident to achieve majority control, as ISS requires that (1) existing directors have clearly failed to perform their duties and (2) the dissident has a viable strategy for improvement

- 2017 study: proxy contests receive 73% more institutional support when ISS supports a measure, 64% when Glass Lewis supports a measure.

- ISS/Glass Lewis recommendations can trigger exceptions to voter agreement provisions in settlements: appears in 39% of all activist settlements in 2018.
Proxy Contest Results

The total number of proxy contests has remained consistent over the past few years:

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Number</th>
<th>Went to Vote</th>
<th>Percentage</th>
<th>Settled/Concessions Made</th>
<th>Percentage</th>
<th>Withdrawn</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>51</td>
<td>17</td>
<td>33%</td>
<td>22</td>
<td>43%</td>
<td>5</td>
<td>10%</td>
</tr>
<tr>
<td>2017</td>
<td>47</td>
<td>17</td>
<td>36%</td>
<td>19</td>
<td>40%</td>
<td>11</td>
<td>23%</td>
</tr>
<tr>
<td>2016</td>
<td>49</td>
<td>15</td>
<td>31%</td>
<td>22</td>
<td>41%</td>
<td>12</td>
<td>25%</td>
</tr>
<tr>
<td>2015</td>
<td>73</td>
<td>26</td>
<td>36%</td>
<td>35</td>
<td>48%</td>
<td>12</td>
<td>16%</td>
</tr>
<tr>
<td>2014</td>
<td>62</td>
<td>14</td>
<td>23%</td>
<td>32</td>
<td>52%</td>
<td>16</td>
<td>26%</td>
</tr>
</tbody>
</table>

Over the last five years, approximately 45% of all proxy contests result in the activist earning a seat. Short slates tend to be more successful than control slates.

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Proxy Contests with Short Slate</th>
<th>Percentage of Proxy Contests with Short Slate</th>
<th>Activist Wins 1+ Board Member (Short Slate)</th>
<th>Number of Proxy Contests with Control Slate</th>
<th>Percentage of Proxy Contests with Control Slate</th>
<th>Activist Wins 1+ Seat (Control Slate)</th>
<th>Activist Wins Majority of Board Seats (Control Slate)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>16</td>
<td>31%</td>
<td>50%</td>
<td>35</td>
<td>69%</td>
<td>46%</td>
<td>9%</td>
</tr>
<tr>
<td>2017</td>
<td>23</td>
<td>49%</td>
<td>52%</td>
<td>24</td>
<td>51%</td>
<td>38%</td>
<td>8%</td>
</tr>
<tr>
<td>2016</td>
<td>13</td>
<td>27%</td>
<td>39%</td>
<td>36</td>
<td>74%</td>
<td>36%</td>
<td>8%</td>
</tr>
<tr>
<td>2015</td>
<td>24</td>
<td>33%</td>
<td>42%</td>
<td>49</td>
<td>67%</td>
<td>39%</td>
<td>8%</td>
</tr>
<tr>
<td>2014</td>
<td>18</td>
<td>29%</td>
<td>67%</td>
<td>44</td>
<td>71%</td>
<td>52%</td>
<td>14%</td>
</tr>
</tbody>
</table>
Trends in Settlement Agreement Terms

- Companies often settle a proxy contest in advance of the vote because of a contest’s disruptive nature, often unpredictable outcome and risk of reputational damage.

- The percentage of settlement agreements between companies and activists filed with the SEC for 2018 increased 18% to 45 from 38 in 2017 (down from a high of 81 in 2015).

- 87% of settlement agreements provide for appointment of one or more board seats.

- Settlement agreements include “standstill” provisions that prevent the activist from engaging in certain activities within a specified period (often one year). Typical prohibited activities include:
  - Proxy solicitation (91%)
  - Publicly disparaging the company or its directors (89%)
  - Seeking board additions/removals (89%)
  - Forming a group or entering into a voting agreement (87%)
  - Presenting a shareholder proposal (85%)
  - Calling a special shareholders meetings (83%)
  - Challenging-seeking waiver from the standstill provisions (72%)
  - Bringing litigation other than enforcing the settlement agreement (65%)
  - Announcing intent to go against settlement agreement (59%)
  - Acquiring more shares (55%)
Key Shareholder Proposals Trends

- Governance and environmental/social/political (ESP) issues, including an increased focus on human capital metrics and efforts to create standardized sustainability reporting, continue to garner significant attention in proposals submitted by shareholders under SEC Rule 14a-8.

- Governance proposals are the most likely type of shareholder proposal to reach a vote and continue to represent the vast majority of proposals that pass (21% all proposals passed in 2019 TYD, up from 2018).
  - Frequent governance proposals in 2019 included proposals regarding:
    - Independent chair
    - Director diversity & qualifications
    - Written consent
    - Supermajority vote requirements
    - Proxy access
    - Special meetings

- ESP proposals continue to gain momentum, with those going to a vote receiving higher support (32%) than previous years and a record 9 proposals passing.
  - Frequent ESP proposals in 2019 included proposals regarding:
    - Political contributions/lobbying
    - Environmental & climate impact
    - Human capital management (gender pay equity, workforce diversity and sexual harassment)
    - Human rights issues
    - Hot button current events (immigration/detention, the opioid crisis)
  - ISS supported 81% of ESP proposals voted on in 2019 YTD, including 94% of political contributions/lobbying proposals and 95% of anti-discrimination proposals. ISS supported 60% of environmental proposals in 2019 YTD.
Activism Preparedness & Response
Activism Preparedness: Before the Activist Emerges

Management and the Board should adopt proactive strategy to anticipate and defend against potential campaigns before an activist appears.

1. **ASSEMBLE AND EDUCATE TEAM**
   - Assemble core response team, including both internal personnel and external advisors (legal, financial, public relations, proxy solicitor)
   - Review structural defenses and governance trends on an annual basis
   - Conduct an annual review with the Board on strategic alternatives and intrinsic value
   - Maintain communications between management and the Board

2. **IDENTIFY VULNERABILITIES**
   - Think like an activist investor
   - Identify areas of potential vulnerability, including governance and financial performance
   - Review charter/by-laws, contracts (change in control provisions, executive compensation)

3. **REMAIN PREPARED AND ANTICIPATE**
   - Take appropriate preemptive actions, including enhancements to structural defenses
   - Formulate a business response plan to an activist investor challenge
   - Develop a communications response plan: public messaging, investor outreach, employee outreach, ISS and other third-party governance reports

4. **MONITOR SHAREHOLDERS**
   - Actively engage and monitor hedge fund and institutional shareholder base – understand their concerns and ensure management communicates regularly to address issues
   - Communicate strategic plan and vision regularly to shareholder base
Activism Response: Best Practices

• A Company has no duty to disclose the emergence of the activist investor (unless the Company or its representatives is the source of a leak)
  • All inquiries should be referred to the CEO to enforce a “one voice” policy

• The Board should continue to meet regularly to discuss the activist situation
  • The Board can delegate day-to-day communications issues to a working group of directors, but the full Board should remain informed

• Keep the Board and management cohesive and energized

• Remain focused on the business – activism campaigns consume time and resources, but strong performance is one of the Company’s best defenses

• Maintain credibility with shareholders, proxy advisory firms and other stakeholders by emphasizing the strengths of the Company’s strategic plan and why the incumbent Board is best equipped to execute against that plan

• Consider whether the Company should take any affirmative actions (e.g., appoint new independent directors) even after the activist has gone public

• Consider whether it is appropriate to enact any defensive measures (e.g., put a poison pill in place), but be careful of ISS’s and investors’ reactions

• With the assistance of the Company’s external advisors, continue to monitor analysts’ reports, media and social media regarding the activism situation
Activism Preparedness: Shareholder Engagement

- Maintain a positive dialogue, relationships and credibility with shareholders, especially key institutional investors and other large shareholders
- Plan ahead – the best time to create a foundation for investor engagement is in between proxy seasons
  - Practicing proactive, consistent investor engagement helps Company understand investor concerns and build credibility
- Articulate a clear strategic plan and vision for creating shareholder value and practicing good governance
- Consider any appropriate changes to the Company’s current governance practices – it may also be a good excuse to reach out to an investor
- Remain alert of developments in shareholder activism and corporate governance more generally
- *Remember to be mindful of Regulation FD during discussions with investors*
- Directors should understand their fiduciary duties and be familiar with the Company’s current defensive posture as well as the Company’s strategic plan
Hypothetical: An Activist Investor Comes Knocking

Part I

- On a clear day, the Company’s CEO receives a call from Mr. X, the head of a prominent activist hedge fund
  - Mr. X informs CEO that his hedge fund has just become one of the Company’s largest shareholders and is about to file an HSR notification regarding its intent to acquire approximately 5.5% of the Company’s stock
  - Mr. X also states his hedge fund will then file a Schedule 13D with the SEC publicly disclosing that it has acquired beneficial ownership of more than 5% of the Company’s stock and intends to engage in discussions with the Company’s board and management
  - Mr. X asks to schedule a meeting with the CEO and members of the Company’s board. Mr. X enthusiastically tells the CEO that the Company has great potential and he would like to share his thoughts on how the Company can further enhance shareholder value
- The CEO immediately calls you, the Company’s General Counsel, to inform you about the call from Mr. X
- What should you do?
Hypothetical: An Activist Investor Comes Knocking

Part II

- The CEO and Chairman of the Board agree to meet with Mr. X to learn as much as possible about Mr. X’s plans for the Company.

- During the meeting, Mr. X discloses that he would like the Company to consider a spin-off of one of its business units and explains why he believes a spin-off is in the best interest of the Company and its shareholders.

- Mr. X states that he is willing to work with the Company privately, but that he is considering nominating three director candidates before the advance notice deadline for the Company’s upcoming annual meeting if he feels that sufficient progress has not been made in advance of the deadline.

- The CEO and Chairman report back to you and the Board regarding the meeting. What should you do next?
Hypothetical: An Activist Investor Comes Knocking

Part III

• The Company and Mr. X engage in further discussions over the next few weeks

• Mr. X is pleased to learn that the Company has agreed to consider a spin-off, but he does not think that the Company is moving fast enough

• The Company and Mr. X discuss a potential settlement, but Mr. X is adamant that (1) he personally serve on the Board and (2) the Company would prefer that a settlement should involve appointing independent directors with industry expertise

• Unfortunately, settlement discussions break down and Mr. X sends an official notice nominating three director candidates (Mr. X and two independents) for election to the Company’s Board at the next annual meeting

• Mr. X also informs the Company that his hedge fund now beneficially owns more than 5% of the Company’s stock and will shortly be filing a Schedule 13D

• What should you do now? How should the Company prepare for a public campaign by the activist?
Hypothetical: An Activist Investor Comes Knocking

Part IV

• The Company and Mr. X’s hedge fund enter into a settlement agreement, pursuant to which Mr. X and an independent director selected by Mr. X are appointed to the Company’s board in exchange for certain standstill protections.

• The Company and its financial advisor conduct a strategic review to investigate the spin-off and other strategic alternatives available to the Company.

• The strategic review is now complete; based on the results, the Company’s financial advisor, senior management and a majority of the Board believe that a spin-off is **not** in the best interests of the Company and its shareholders.

• Mr. X and the new independent director disagree with this decision and continue to support a spin-off.

• How does the Board navigate this conflict? What should the Company do next?

• **More generally, how does the company navigate its relationship with the activist investor once the activist has a presence on the board?**
2019 Proxy Season Review: Part 1
Rule 14a-8 Shareholder Proposals

Focus on environmental, social and political (ESP) proposals intensifies:
- Although total submitted ESP proposals decrease, voted ESP proposals sharply increase as a percentage (to nearly half), receive record level of support (over 30% average support) and pass in record number (nine)
- Half of workplace diversity proposals reach a vote and shareholder support remains high (almost 40%)
- Nine out of ten top submitters submit double-digit ESP proposals

Prior trends relating to governance proposals continue:
- Governance proposals down from 2018, continuing a trajectory from 2015 (led by 66% reduction in special meeting-related proposals)
- Although fewer in number, proposals to reduce special meeting thresholds continue to receive high support (averaging 44%), with four passing (the same as last year)
- Independent chair is most common governance proposal, although none pass and ISS support decreases

Growth in proposals against investing on the basis of ESP factors (so-called anti-ESP proposals) affects overall trends in both ESP and governance proposals
INTRODUCTION

Our annual proxy season review memo summarizes significant developments relating to the 2019 U.S. annual meeting proxy season. This year our review comprises three parts: Rule 14a-8 shareholder proposals submitted and voted, ISS negative recommendations and compensation-related matters. This is Part 1, and we expect to issue Parts 2 and 3 over the next several weeks. Details regarding our annual webinar to discuss 2019 proxy season developments will be disseminated later this summer.

The Rule 14a-8 shareholder proposals we discuss are those submitted to and/or voted on at annual meetings of the U.S. members of the S&P Composite 1500, which covers over 90% of U.S. market capitalization, at meetings held on or before June 30, 2019. We estimate that around 90% of U.S. public companies held their 2019 annual meetings by that date.

The data on submitted, withdrawn and voted-on shareholder proposals derives from ISS’s voting analytics with respect to about 678 known shareholder proposals submitted this year to U.S. members of the S&P Composite 1500. We have supplemented the ISS data with information published by proponents on their websites and other independent research. The number of proposals submitted includes proposals that were withdrawn before or after being included in a company’s proxy statement (usually following engagement with the company) or excluded from a company’s proxy statement through the SEC no-action process. The data on submitted proposals understates the number of proposals submitted, as it generally does not include proposals that were submitted and then withdrawn unless either the proponent or the company voluntarily reported the proposal to ISS or on their websites.

For a discussion of U.S. proxy contests and other shareholder activist campaigns, see our publication, dated March 14, 2019, entitled “Review and Analysis of 2018 U.S. Shareholder Activism.”

More generally, for a comprehensive discussion of U.S. public company governance, disclosure and compensation, see the Public Company Deskbook: Complying with Federal Governance and Disclosure Requirements (Practising Law Institute) by our colleagues Bob Buckholz and Marc Trevino, available at 1-800-260-4754 (1-212-824-5700 from outside the United States) or http://www.pli.edu.
# Table of Contents

A. Overview of Shareholder Proposals ................................................................. 1
B. Who Makes Shareholder Proposals .................................................................. 4
C. Targets of Shareholder Proposals .................................................................... 6
D. Shareholder Proposals on Environmental/Social/Political Matters ................... 7
   1. Political ........................................................................................................ 8
   2. Environmental ............................................................................................. 10
   3. Human Capital ............................................................................................. 11
E. Shareholder Proposals on Governance Matters .................................................. 15
   1. Independent Chair ..................................................................................... 18
   2. Board Composition .................................................................................... 19
   3. Shareholder Right to Act by Written Consent ............................................. 25
   4. Elimination of Supermajority Thresholds, Majority Voting in Uncontested Elections and Board Declassification ................................................................. 26
   5. Proxy Access Proposals .............................................................................. 27
   6. Shareholder Right to Call Special Meetings ................................................ 28
   7. Dual Class Voting ....................................................................................... 31
   8. Other Governance Proposals ....................................................................... 32
F. Compensation-Related Shareholder Proposals .................................................... 34
G. No-Action Relief .............................................................................................. 37
   1. Ordinary Business ....................................................................................... 37
   2. Substantial Implementation .......................................................................... 39
   3. Conflicting Management Proposals ............................................................. 39
H. Exempt Solicitations ......................................................................................... 41
PART 1. RULE 14A-8 SHAREHOLDER PROPOSALS

A. OVERVIEW OF SHAREHOLDER PROPOSALS

The following table and pie charts summarize, by general category, the Rule 14a-8 shareholder proposals submitted in 2018 full-year and 2019 year-to-date, the number voted on and the rate at which they passed.\(^1\) Overall, the total number of shareholder proposals significantly declined, continuing a downward trend from 2015. A total of 678 shareholder proposals have been submitted to-date in 2019, relative to 751 at this time last year, 788 for 2018 as a whole and 836 for 2017. The decline relative to this time last year is led by a 12.5% drop in environmental, social, and political ("ESP") proposals, closely followed by compensation-related proposals (11.9% drop), with governance-related proposals declining by a smaller proportion (6.2% drop).\(^2\) The overall decline would have been steeper but for the increase in proposals against investing or managing on the basis of ESP factors (so-called anti-ESP proposals).

**SUMMARY OF 2018-2019 SHAREHOLDER PROPOSALS**

<table>
<thead>
<tr>
<th>Type of Proposal</th>
<th>2019 YTD</th>
<th>2018</th>
<th>2019 YTD</th>
<th>2018</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ESP</td>
<td>323</td>
<td>387</td>
<td>146</td>
<td>139</td>
<td>28%</td>
<td>9</td>
</tr>
<tr>
<td>Governance-related</td>
<td>303</td>
<td>335</td>
<td>195</td>
<td>234</td>
<td>37%</td>
<td>41</td>
</tr>
<tr>
<td>Compensation-related</td>
<td>52</td>
<td>66</td>
<td>30</td>
<td>42</td>
<td>24%</td>
<td>2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>678</strong></td>
<td><strong>788</strong></td>
<td><strong>371</strong></td>
<td><strong>415</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\(^1\) In this publication, when we refer to a proposal as “passing,” we mean that it received the support of a majority of votes cast, regardless of whether this is the threshold for shareholder action under state law or the company’s bylaws. Unless stated otherwise, we refer to proposals withdrawn by the proponent either before or after the mailing of a company’s proxy materials, as well as proposals which are not presented by the proponent at the shareholder meeting, as “withdrawn.” We refer to proposals that have been excluded through the SEC no-action process as “excluded.”

\(^2\) Although commenters often group governance matters together with environmental and social matters (referred to as ESG), separating governance and ESP matters provides additional insight in the context of discussing shareholder proposals.
Despite the drop year-over-year, more ESP proposals were submitted than any other type of shareholder proposal for the third year in a row. This year nearly half of submitted ESP proposals went to a vote, while in 2018 only about a third reached the shareholder vote stage.

Very few ESP proposals actually passed, as was the case in 2017 and 2018, although shareholder support for ESP proposals has increased steadily over both the long- and short-term. Average shareholder support for ESP proposals reached 28% this year, continuing the upward trend from less than 10% ten years ago to 26% in 2018. The gap in the average support rate between ESP and governance-related proposals also continued to narrow, down to nine percentage points from 11 percentage points in 2018 and 17 percentage points in 2017. ESP proposals are discussed in more detail in Section D.

The number of governance-related proposals fell 6.2% compared to the same time last year, as companies continued proactive adoption of practices that have become market standard (e.g., proxy access), and proponents continued to explore those areas where market practice has not settled (e.g., independent board chair).

As was the case in 2018, governance-related proposals were the most likely to reach a vote (64.4% in 2019; 69.9% in 2018) and continued to represent the vast majority of proposals that actually passed. The percentage of proposals that passed in 2019 (21% of voted proposals) increased from 2018 (13% of voted), primarily due to an increase in the number of elimination of supermajority thresholds proposals that came to a vote and that passed (19 and 16 in 2019, respectively, compared to 11 and 9 in 2018). Governance-related proposals are discussed in more detail in Section E.

The number of compensation-related proposals remained at a negligible level, continuing a trend that began when mandatory say-on-pay votes came into effect. As was the case in 2018, the most common proposal topic is tying ESP performance to compensation targets (34.6% of all compensation-related proposals submitted, compared to 36.4% in 2018). Whereas no compensation-related proposals passed in 2018, two proposals (both related to clawbacks) passed in 2019. Compensation-related proposals are discussed in more detail in Section F.
SULLIVAN & CROMWELL LLP

B. WHO MAKES SHAREHOLDER PROPOSALS

The focus of a relatively concentrated group of individuals and entities continues to drive the voting agenda at U.S. public companies. The top ten proponents account for more than half of shareholder proposals submitted to U.S. S&P Composite 1500 companies. This year, with the exception of John Chevedden, Kenneth Steiner, and James McRitchie/Myra Young, all of the top proponents submitted a greater number of ESP proposals than governance-related proposals, including the public pension funds. It is worth noting that reporting on the filer of a shareholder proposal camouflages the even more robust activity this year from investor coalitions (such as the National Center for Public Policy Research and the Interfaith Center on Corporate Responsibility), which submit proposals through individual members. It appears that the concentration of proposals would be even higher if aggregated at the coalition level.

The following table shows a breakdown of the types of proposals submitted by the top shareholder proponents in 2019:

<table>
<thead>
<tr>
<th>Primary or Secondary Filers3</th>
<th>ESP</th>
<th>Governance</th>
<th>Compensation</th>
<th>Total</th>
<th>% of All Proposals</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 John Chevedden</td>
<td>10</td>
<td>134</td>
<td>0</td>
<td>144</td>
<td>23%</td>
</tr>
<tr>
<td>2 NYC Comptroller</td>
<td>33</td>
<td>15</td>
<td>4</td>
<td>52</td>
<td>8%</td>
</tr>
<tr>
<td>3 As You Sow Foundation</td>
<td>46</td>
<td>4</td>
<td>2</td>
<td>52</td>
<td>8%</td>
</tr>
<tr>
<td>4 James McRitchie/Myra Young</td>
<td>13</td>
<td>30</td>
<td>2</td>
<td>45</td>
<td>7%</td>
</tr>
<tr>
<td>5 Kenneth Steiner</td>
<td>0</td>
<td>44</td>
<td>0</td>
<td>44</td>
<td>7%</td>
</tr>
<tr>
<td>6 Mercy Investment Services</td>
<td>32</td>
<td>1</td>
<td>6</td>
<td>39</td>
<td>6%</td>
</tr>
<tr>
<td>7 NYS Common Retirement Fund</td>
<td>24</td>
<td>0</td>
<td>4</td>
<td>28</td>
<td>4%</td>
</tr>
<tr>
<td>8 Sisters of St. Francis</td>
<td>19</td>
<td>3</td>
<td>2</td>
<td>24</td>
<td>4%</td>
</tr>
<tr>
<td>9 Trillium Asset Management</td>
<td>13</td>
<td>12</td>
<td>2</td>
<td>27</td>
<td>4%</td>
</tr>
<tr>
<td>10 Arjuna Capital</td>
<td>18</td>
<td>1</td>
<td>0</td>
<td>19</td>
<td>3%</td>
</tr>
</tbody>
</table>

- **Individuals.** Three of the five most prolific proponents were the individual investors who have been prominent for a number of years: John Chevedden, Kenneth Steiner, and James McRitchie/Myra Young. Collectively, these individuals and their family members were responsible for the submission of 233 proposals. These individuals often submit proposals jointly as co-filers. Without counting overlaps, these individuals submitted 210 unique proposals in 2019 so far. Overall, they represented 31% of all proposals submitted (up from about 27% in 2018) and the clear majority of governance-related proposals (62%, up from about 58% in 2018). For the first time since we began tracking total submissions, this group submitted a meaningful number of ESP proposals, with 20 unique ESP proposals submitted in 2019 to date (compared to six in all of 2018), most of which related to political contributions (all of the ESP proposals submitted by John Chevedden related to disclosure on political contributions, most of which reached a shareholder vote). In December, James McRitchie announced that he and his wife, Myra Young, would turn their attention to collaborations with As You Sow Foundation and the Center for Political Accountability as proponents for proposals in the ESP area.

---

3 Based on ISS records of the named sponsors of shareholder proposals, which we have supplemented with information published by proponents on their websites and other independent research.

2019 Proxy Season Review
Part 1 – Rule 14a-8 Shareholder Proposals
Social Investment Entities. The majority of ESP proposals continued to come from asset management or advisory institutions that seek to make “socially responsible” investments and advance social causes. The entities that were most active in 2019 included As You Sow Foundation (46 ESP proposals submitted), Mercy Investment Services (32), Arjuna Capital (18), and Trillium Asset Management (13). This year, a meaningful number of proposals came from “anti-ESP” entities such as Burn More Coal, a special interest group supportive of the coal industry, and the Free Enterprise Project, the conservative shareholder activist arm of the National Center for Public Policy Research (NCPPR), as further discussed in Sections D and E.

Religious Organizations. This year, religious organizations also submitted a meaningful number of ESP proposals (focusing on environmental, human capital and human rights) and proposals targeting companies in the pharmaceutical, healthcare and financial services sectors. Many of the active religious organizations were affiliated with the faith-based investor coalition, the Interfaith Center on Corporate Responsibility (ICCR). Among other initiatives, ICCR has teamed up with the Investors for Opioid Accountability (IOA), a 54-member coalition of global institutional investors with $3.5 trillion in assets under management established to engage opioid manufacturers. This year, IOA focused on independent chair, board level responsibility for opioid business risk oversight, misconduct clawback policies, exclusion of legal/compliance costs from compensation metrics, and expanded disclosure in connection with the opioid crisis. In significant part due to the engagement of IOA, ICCR and their affiliates, this year, at least ten pharmaceutical companies have included proposals in their proxy statements related to the opioid epidemic, and a number of other proposals reference opioid-related issues at the company to support governance and/or compensation reforms. Several healthcare and pharmaceutical companies, including Healthstream, Siga Technologies and Eagle Pharmaceuticals, have also began to include in their proxy statements director qualifications relating to the management of the opioid crisis.

Public Pension Funds and Entities. Public sector pension funds and entities proposed 79 unique proposals to public companies for 2019 meetings. The most frequent proponent in this category was the New York City Comptroller (with 52 proposals submitted). Topics commonly addressed by proposals from pension funds and other public sector entities include political contributions and lobbying, management of human capital, and environmental matters.

Labor Unions. Labor unions, such as the AFL-CIO and the Teamsters, were the proponents of 32 unique proposals, with ESP as the most popular issue, and then evenly spread between governance- and compensation-related issues.

The ability of shareholders with a relatively small investment in the company ($2,000 of stock held for one year) to submit Rule 14a-8 proposals has been a subject of controversy and calls for change in recent years. Although congressional attempts to increase the investment threshold for submission or to curtail resubmission of proposals have fallen short, such amendments are currently one of the SEC’s stated near-term priorities. At a roundtable on proxy process that the SEC hosted in November 2018, the current thresholds for filing shareholder proposals was a main topic under consideration, with participants discussing whether the current thresholds, or more rigorous thresholds, are appropriate in light of the interests of all shareholders. On May 22, 2019, the SEC released its Regulatory Flexibility Agenda, which includes plans to consider amendments to the Rule 14a-8 thresholds. Although the agenda does not address the specific changes the SEC expects to make, it does indicate that the SEC intends to release advanced notice of proposed rule-making by April 2020.
C. TARGETS OF SHAREHOLDER PROPOSALS

Traditionally, large-cap companies have received the vast majority of shareholder proposals. In 2019 so far, S&P 500 companies received nearly 82% of proposals voted on, consistent with levels in 2018 (83%).

The following graphs show the frequency of proposals, by category, voted on at large-cap companies compared to small- and mid-cap companies. The higher numbers at large-cap companies are particularly notable given that the small-/mid-cap graph includes twice as many companies.

---

4 In this publication, we use “large-cap” to mean U.S. S&P 500 companies, “mid-cap” to mean U.S. S&P 400 companies, and “small-cap” to mean U.S. S&P 600 companies.
D. SHAREHOLDER PROPOSALS ON ENVIRONMENTAL/SOCIAL/POLITICAL MATTERS

ESP proposals continued to gain momentum, with the ESP proposals that went to a vote receiving record average support of 28% and a record nine proposals passing. Unlike governance proposals, which have high support concentrated in a limited number of topics, support across a variety of ESP topics was relatively consistent. The proposals that did register substantially lower voter support related to requests that were in direct contradiction with the company’s business (e.g., proposing The Coca-Cola Company report on the deleterious health impact of processed sugar, or requesting Altria Group, Inc. reduce nicotine levels in tobacco products) or were so-called anti-ESP proposals (e.g., proposing that Duke Energy report on the costs of voluntary environment-related activities).

<table>
<thead>
<tr>
<th>ESP PROPOSALS</th>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Voted On</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Political</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Environmental</td>
<td>93</td>
<td>93</td>
<td>59</td>
<td>55</td>
</tr>
<tr>
<td>Human capital</td>
<td>64</td>
<td>110</td>
<td>20</td>
<td>34</td>
</tr>
<tr>
<td>Human rights</td>
<td>54</td>
<td>59</td>
<td>30</td>
<td>13</td>
</tr>
<tr>
<td>Sustainability report</td>
<td>40</td>
<td>35</td>
<td>14</td>
<td>11</td>
</tr>
<tr>
<td>Health and safety</td>
<td>24</td>
<td>21</td>
<td>4</td>
<td>6</td>
</tr>
<tr>
<td>Animal rights</td>
<td>11</td>
<td>10</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>ESP – other</td>
<td>8</td>
<td>8</td>
<td>1</td>
<td>1</td>
</tr>
</tbody>
</table>

The percent of ESP proposals voted rose sharply to 45.2% from 35.9% in full-year 2018. As a result, the number of ESP proposals voted on is higher than the same period last year, notwithstanding the 12.5% drop in the number of ESP proposals submitted in the first half of 2019 compared to the same period in 2018 (16.5% drop compared to full-year 2018).5

---

5 We note that the submission and withdrawal data generally excludes shareholder engagement prior to the receipt of a formal proposal, which may obscure trends in shareholder engagement with respect to at least some categories of proposals.
The ten shareholder proponents referenced in Section B submitted about two-thirds of all ESP proposals received by U.S. S&P Composite 1500 companies. Among these proponents, As You Sow Foundation submitted the greatest number of ESP proposals (46), most of which related to climate change and reducing the company’s carbon footprint, the majority of which was withdrawn. Arjuna Capital (18), Mercy Investment Services (32), Sisters of St. Francis (19) and Trillium Asset Management (13) also submitted a meaningful number of ESP proposals, particularly focusing on environmental issues and political contributions. Companies resolved about half of the proposals brought by these proponents outside of a shareholder vote, but almost all of the proposals brought by Arjuna went to a vote (most of these were proposals to disclose an unadjusted gender pay gap and are further discussed in Section D.3.a). Although social investment entities and religious groups submitted the bulk of ESP proposals, as was the case in 2018, ESP proposals also represented a larger portion of the submissions this year from other types of proponents, such as public pension funds. For example, over half of all proposals submitted by the NYC Comptroller this year have been ESP proposals.

### 2019 YTD Withdrawal Rates for ESP Proposals (By Top ESP Proponents)

<table>
<thead>
<tr>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Submitted</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019 YTD</td>
<td>2018</td>
<td>2019 YTD</td>
<td>2018</td>
</tr>
<tr>
<td>93</td>
<td>93</td>
<td>59</td>
<td>55</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2019 YTD</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2019 YTD</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2018</td>
</tr>
</tbody>
</table>

Political contributions and lobbying became the most common ESP topic in 2019, representing 28.8% of ESP proposals in 2019, increasing from 24.0% in 2018. The majority of proposals were requests for companies to disclose their political spending (expenses and/or policies), including contributions to candidates, lobbying expenditures and related policies. One notable proposal was a shareholder request
at Intel to allow annual advisory votes on political contributions, which received only 6% of votes cast. Last year, some companies (including Duke Energy and General Electric) received proposals to disclose a report on the benefits and costs of lobbying and/or political spending, which was not the main topic of any proposal this year, perhaps due to the generally low support for these proposals in 2018. Many of the companies that received a political proposal this year were high-profile American brands (such as Macy’s, Disney, Ford, and UPS) or companies in sectors that attract public attention every election year or due to recent sociopolitical events (such as the banking, healthcare, pharmaceutical, insurance, energy, and steel sectors).

Political contributions and lobbying proposals were the most likely to reach a vote among ESP proposals (63.4% in 2019, slightly up from 59.1% in 2018). For the political proposals that reached a vote, the average shareholder support increased to 34% from 29% in 2018 (ISS supported 95%, consistent with 2018).

Before this year, no political proposal had passed since 2016. This year, four political proposals passed, the highest number of passed proposals on any ESP topic. Of these proposals, the proposal to drug maker Mallinckrodt from a coalition of investors led by United Church Funds received the highest shareholder support at approximately 80% of votes cast. In their supporting statements for the proposal (which demanded that the company make annual reports on its lobbying policies, activities and expenditures, and membership in any organization that writes and endorses legislation), the proponents emphasized their concern over the reputational implications of Mallinckrodt’s lack of lobbying disclosure, citing “the heightened media scrutiny” on pharmaceutical companies’ political donations and membership in certain political nonprofits in light of the opioid epidemic. Mallinckrodt supported the shareholder proposal, stating in its proxy that it was already planning to disclose a “Political Engagement Report” covering similar topics, which it intends to update annually. Similar to the proposal at Mallinckrodt and many political proposals submitted by shareholders in recent years, the proposals that passed at Alliant, Cognizant and Macy’s emphasized the importance of transparent disclosure to shareholders on a company’s direct and indirect political expenditures, non-monetary contributions, and affiliation with political nonprofits, citing the Supreme Court’s *Citizens United* decision for the proposition that “disclosure permits citizens and shareholders to react to the speech of corporate entities in a proper way.” At Alliant, a utilities company, the proponent, the NYC Comptroller, also highlighted that many of the company’s industry peers publicly disclose political spending. The proposals that passed at Alliant, Cognizant and Macy’s were opposed by the respective company’s board, and received just over 50% of votes cast (54%, 54% and 53%, respectively). In their response statements, each board expressed the concern that expanded disclosures could place the company at a competitive disadvantage and that the disclosure of indirect political activities, including membership in various trade organizations, may misrepresent their respective companies’ actual political activities, since these organizations take independent action with which the board may disagree. This year, political proposals at 17 other companies received over 40% of
SULLIVAN & CROMWELL LLP

voters cast, including at three other consumer/retail companies (49.8% at Kohl’s, 42.4% at Honeywell, and 41.7% at Netflix) and two other utilities companies (48.7% at NextEra Energy and 45.4% at NRG Energy).

2. Environmental

<table>
<thead>
<tr>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Voted On</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019 YTD</td>
<td>2018</td>
<td>2019 YTD</td>
<td>2018</td>
</tr>
<tr>
<td>Greenhouse gas emissions</td>
<td>15</td>
<td>32</td>
<td>6</td>
</tr>
<tr>
<td>Cost of environmental activities</td>
<td>4</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>Board oversight</td>
<td>3</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>Environmental – other</td>
<td>42</td>
<td>74</td>
<td>10</td>
</tr>
</tbody>
</table>

This year, there was a significant drop in the number of environmental proposals (64 in 2019, compared to 110 in 2018), but the percentage of proposals that went to a vote this year was level with 2018 (31.3% in 2019, compared to 30.9% in 2018). For the first time since 2015, no environmental proposal passed (compared to five in 2018).

Environmental proposals had been the most common ESP topic in both 2017 and 2018 but were in second place this year. In 2018, following President Trump’s June 2017 announcement that the United States was withdrawing from the Paris Agreement, shareholders submitted a number of proposals requesting that companies (particularly in the energy and manufacturing sectors) report on the alignment between their environmental goals and the goals set out in the Paris Agreement, in particular with respect to greenhouse gas emissions targets. Accordingly, last year, there were close to 70 proposals submitted that related to the goals of the Paris Agreement, including 32 greenhouse gas emissions-related proposals. This year, fewer than 30 submitted proposals related to the goals of the Paris Agreement, with only 15 proposals on greenhouse gas emissions targets.

On aggregate, average shareholder support for environmental proposals decreased, dropping from 31% in 2018 to 24%, with ISS support for environmental proposals dropping from 85% in 2018 to 60%. Adjusting for the two anti-ESP environmental proposals that reached a vote, however, the 2019 average shareholder and ISS support rates were aligned with the 2018 levels, at around 31% and 90%, respectively. ISS recommended against both voted anti-ESP proposals to report on the cost of taking voluntary environmental actions (one from Burn More Coal at Exelon and one citing Burn More Coal at Duke Energy, receiving 1.6% and 4.4% of votes cast, respectively). Two anti-ESP proposals at Exxon (one to disclose the costs of environmental activities and one to adopt a policy not to undertake projects based on climate change concerns) were excluded through the SEC no-action process on the basis of substantial implementation.
In addition to recommending against the anti-ESP proposals, ISS recommended against six other environmental proposals this year, including two voted proposals that called for greater board oversight of environmental issues (the two voted proposals called for the establishment of a new environmental committee on the boards of Exxon and Chevron; another proposal, which requested that PNM Resources nominate a director with climate change experience, was excluded through the SEC no-action process on the basis of substantial implementation). ISS recommended against environmental proposals at Mondelez, PepsiCo, Exxon and DuPont to report on certain specific issues, such as deforestation, pesticide management, petrochemical operations in flood-prone areas, and efforts to reduce plastic pellet pollution, noting that these companies already provide industry-standard environmental disclosures.

3. Human Capital

<table>
<thead>
<tr>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Voted On</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gender/other pay gap</td>
<td>26</td>
<td>30</td>
<td>13</td>
</tr>
<tr>
<td>Workplace diversity</td>
<td>17</td>
<td>25</td>
<td>8</td>
</tr>
<tr>
<td>Sexual harassment</td>
<td>7</td>
<td>0</td>
<td>5</td>
</tr>
<tr>
<td>Human capital – other</td>
<td>4</td>
<td>4</td>
<td>4</td>
</tr>
</tbody>
</table>

Shareholders began to submit a meaningful number of proposals related to management of human capital for the first time in 2018, driven in part by the momentum of the #MeToo, #TimesUp and similar movements. This year, proposals related to management of human capital remained the third largest category of ESP proposals submitted (16.7% of all ESP proposals submitted, compared to 15.2% in 2018), as shareholders, proxy advisors and the public continued to focus on topics such as gender pay equity, workplace diversity, and sexual harassment. However, compared to 2018, when companies that received such proposals generally reached a compromise with the proponent in advance of the shareholder voting stage, over half of these proposals went to a vote this year (55.6% in 2019, compared to 22.0% in 2018). The increase in the percentage of voted-on proposals is due in part to proposals requesting additional disclosure from companies already providing some disclosures on the relevant topic (particularly with respect to gender pay gap), either proactively or in response to a prior shareholder proposal.

More companies are likely to adopt or expand public disclosure on human capital management in response to growing pressure from investors and regulators. For example, the SEC’s Investment Advisory Committee voted 14 to 6 in March 2019 to recommend that the SEC consider as a part of the SEC’s Disclosure Effectiveness Review imposing a requirement on public companies to make disclosures relating to human capital management disclosure. In his opening remarks, Chairman Jay Clayton emphasized that human capital “is a mission-critical asset” but that making appropriate rules and
guidance around human capital management disclosure is not a simple task due to sector- and company-
specific factors.

a. Gender Pay Gap

This year, proposals on pay-gap disclosures once again comprised around half of submitted proposals
related to management of human capital, as lawmakers, courts, shareholders, the media and the general
public continue to focus on pay equity, particularly the gender pay gap. Although the global World
Economic Forum has reported in its Global Gender Gap Report 2018 that the economic gender gap
narrowed slightly in 2018, it also suggested that it would take 108 years to close the global gender gap at
the current rate of change. In the United States, the public spotlight on the gender pay gap has intensified
as the 2020 presidential election approaches. Multiple candidates from the Democratic Party have
endorsed legislation and policies intended to close the national wage gap, which was at a median of
18.9% in 2018 according to data from the Institute for Women’s Policy Research. Earlier this year, House
Speaker Nancy Pelosi and other Democratic Congressional leaders reintroduced the Paycheck Fairness
Act, a bill first proposed in 1997 with the goal of increasing pay-equity protections for women and
strengthening the Equal Pay Act of 1963 by, among other things, requiring employers that compensate
employees differently for performing the same job to justify the discrepancy, and eliminating pay secrecy.
The bill passed the House in March and now sits in the Senate. New York, Delaware, Oregon, California
and Massachusetts have also adopted laws that increase pay-equity protections, including prohibiting
employers from asking about a candidate’s wage history, while other states are considering similar
legislative steps. Studies show popular support, particularly among women, for legislation that would
mandate that companies disclose gender pay-gap data, a policy position that has become a priority for a
number of federal lawmakers and presidential candidates; similar legislation has been adopted in the U.K.
and Germany in recent years.

In parallel with these legislative efforts, shareholders continued to apply pressure on companies to
disclose voluntarily pay-gap information, primarily focusing on the gender pay gap. This year, shareholder
proposals relating to pay-gap reporting represented half of all human capital proposals, similar to 2018.
The New York City Comptroller and Arjuna Capital, a social investment entity, submitted the majority of
these proposals. The recipients of these proposals were predominately in the financial services and
technology sectors.

This year, the majority of proposals on the gender and/or racial pay gap failed to reach a vote, as was the
case in 2018, in many cases following private engagement between the company and the proponent.
However, a far higher percentage of these proposals went to a vote (50% in 2019 compared to 20% in
2018). Proposals from Arjuna Capital represented all but two of the voted proposals. In each case,
Arjuna Capital requested that the company, which already reports its pay gap on a statistically adjusted
equal pay basis, disclose the unadjusted global median pay-gap figures as well. (Between 2016 and
2018, Arjuna Capital had successfully engaged with 22 companies to publish their gender pay-gap figures
on an adjusted basis, including some of the companies that received a proposal this year to publish unadjusted figures.) In the supporting statements for their proposals this year, Arjuna Capital argued that statistically adjusted numbers, which reflect pay disparity between employees at similar roles, levels and/or geographies, fail to consider how discrimination affects differences in job and advancement opportunity, and that disclosure of the global median pay gap would better highlight the structural biases that affect the jobs women hold, particularly at higher-paying ranks. In response, boards generally expressed the view that median figures are misleading, because they involve too much abstraction, and emphasized other corporate initiatives to examine and/or report on the fairness of advancement opportunities across demographic groups. In addition, Bank of America and Wells Fargo tried to exclude the Arjuna Capital proposals they received, but the SEC rejected each company’s argument that the proposal amounted to “micromanagement” to justify an exclusion under Rule 14a-8(i)(7).

Arjuna Capital only withdrew one pay-gap proposal this year, at Citigroup (in contrast, the pay-gap proposals submitted by the New York City Comptroller, which seemed to focus on companies that did not report on gender pay gap, were all withdrawn before a vote). Earlier this year, Citigroup became the first U.S. company to disclose a global median pay gap that was not adjusted for job function, level, or geography. Notably, Citigroup’s unadjusted data reflected a 29% gap between male and female employees, whereas it had disclosed a 1% gender pay gap on an adjusted basis in 2018. Arjuna Capital withdrew its shareholder proposal after Citigroup’s disclosure and commended Citigroup for “this new level of transparency that provides investors with baseline metrics to understand broad pay equity at the company.”

In April, Arjuna Capital and Proxy Impact issued a report card ranking 46 prominent companies on gender and racial pay equity, and the only company that received an “A” was Citigroup. Although none of the eleven voted proposals from Arjuna Capital passed, three received support above 30% of votes cast, and one of the other two voted pay-gap proposals, a proposal at Cigna from Proxy Impact, which addressed an identical issue and provided similar reasoning, also received over 30% of votes cast (the other voted pay-gap proposal was a request at The TJX Companies from Zevin Asset Management to generally report on the company’s policies and goals for reducing pay inequities, which received 18.4% of votes cast). Shareholder support may further increase in the future. Given the significant shareholder support for many of its proposals and its stated goal of increasing transparency with respect to pay disparity, Arjuna Capital is likely to continue requesting companies to disclose unadjusted figures and is unlikely to accept a compromise short of the requested disclosure.

---


2019 Proxy Season Review
Part 1 – Rule 14a-8 Shareholder Proposals

-13-
b. Workplace Diversity

The number of workplace diversity proposals fell by more than half relative to 2018. The proposals submitted, which requested companies to report on workplace diversity metrics and policies, were predominantly sponsored by Trillium Asset Management. This year, 47.1% of these proposals reached a vote, representing a significant increase from 2018, when 24% reached a vote. Shareholder support for these proposals remained high (at 35% in 2019, relative to 41% in 2018). The eight voted workplace diversity proposals included repeat proposals at Charles Schwab, Home Depot and Travelers to report on diversity along EEOC identified categories, which received a substantial amount of shareholder support in both 2019 and 2018 (39.8%, 33.1% and 50.9%, respectively, in 2019, compared to 35.8%, 48.3% and 36.4%, respectively, in 2018).

In addition to the repeat proposal at Travelers, which passed at 50.9% of votes cast this year, a proposal at Newell Brands to report on the diversity of the company’s executive leadership team passed this year with 56.6% of votes cast (in 2018, no workplace diversity proposal passed). In the supporting statement for its proposal at Newell Brands, Trillium Asset Management highlighted the limited racial/ethnic diversity on the company’s highest management committees and that only 11% of the committee members were women. In a 2019 blog post, Trillium Asset Management stated that its goal for submitting similar proposals to Newell Brands and other companies was for the companies to assess “diversity in senior leadership ranks and clear plans to expand diversity, inclusive of gender, race and ethnicity” and “set goals, measure and report progress, and hold executives accountable to improving diversity and inclusion in senior roles.” In addition to requesting companies to report on current diversity, Trillium Asset Management also hinted that it might submit further proposals linking diversity performance metrics to senior executive compensation, expressing in its supporting statements for the workplace diversity proposals that diversity-linked compensation packages can “sharpen management’s ability to manage human capital management risks, increase accountability and successfully reach inclusion and diversity goals.”

c. Sexual Harassment

This year, in parallel with legislative efforts to strengthen sexual harassment prevention (including the recent adoption by New York State and New York City of laws that require employers to conduct annual, interactive sexual harassment training for all employees by October 2019), there were seven shareholder proposals (at Alphabet, Amazon, CBS, Xenia Hotels, Pebblebrook Hotel Trust, Walmart and XPO Logistics) specifically addressing voluntary reporting on sexual harassment and/or policies to strengthen sexual harassment prevention in the workplace. Five reached a vote and averaged 17% shareholder support.
E. SHAREHOLDER PROPOSALS ON GOVERNANCE MATTERS

The number of proposals on governance matters (board-related and anti-takeover concerns) that came to a vote in 2019 was down significantly from 2018, continuing a trajectory from 2015. Proposals on independent chair, board composition, supermajority vote requirements, and majority voting in uncontested elections increased year-over-year. These increases did not offset the significant drop in special meeting-related proposals, the most common governance-related topic in 2018. Average support for governance-related proposals in 2019 was 37% overall, level with 2018 but representing a decrease from prior years.

<table>
<thead>
<tr>
<th>Governance Proposals</th>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Voted On</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Independent Chair</td>
<td>62</td>
<td>54</td>
<td>54</td>
<td>47</td>
</tr>
<tr>
<td>Board Composition</td>
<td>39</td>
<td>30</td>
<td>9</td>
<td>6</td>
</tr>
<tr>
<td>Board Diversity</td>
<td>32</td>
<td>27</td>
<td>9</td>
<td>3</td>
</tr>
<tr>
<td>Director Qualifications</td>
<td>7</td>
<td>3</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>Act by Written Consent</td>
<td>38</td>
<td>41</td>
<td>33</td>
<td>36</td>
</tr>
<tr>
<td>Eliminate Supermajority Thresholds</td>
<td>37</td>
<td>26</td>
<td>19</td>
<td>11</td>
</tr>
<tr>
<td>Proxy Access</td>
<td>33</td>
<td>47</td>
<td>27</td>
<td>35</td>
</tr>
<tr>
<td>Adopt new right</td>
<td>11</td>
<td>18</td>
<td>5</td>
<td>10</td>
</tr>
<tr>
<td>Amend existing right</td>
<td>22</td>
<td>29</td>
<td>22</td>
<td>25</td>
</tr>
<tr>
<td>Special Meeting</td>
<td>26</td>
<td>77</td>
<td>21</td>
<td>61</td>
</tr>
<tr>
<td>Adopt New Right</td>
<td>1</td>
<td>18</td>
<td>1</td>
<td>8</td>
</tr>
<tr>
<td>Lower % on Existing Rights</td>
<td>25</td>
<td>59</td>
<td>20</td>
<td>53</td>
</tr>
<tr>
<td>Majority Voting in Uncontested Elections</td>
<td>12</td>
<td>7</td>
<td>7</td>
<td>3</td>
</tr>
<tr>
<td>Dual Class Voting</td>
<td>7</td>
<td>11</td>
<td>6</td>
<td>10</td>
</tr>
<tr>
<td>Declassify Board</td>
<td>7</td>
<td>8</td>
<td>4</td>
<td>5</td>
</tr>
</tbody>
</table>

Unlike ESP proposals, when governance proposals failed to reach the shareholder vote stage, it was most often due to exclusion through the SEC no-action process, as the following chart illustrates:
As so-called shareholder-friendly governance features have become standard at S&P 500 companies, a number of governance proposals that previously have dominated proxy seasons and garnered high support from investors (e.g., destaggered boards, majority election of directors, special meeting rights, simple majority vote thresholds and, more recently, proxy access) have become much less prevalent. There are simply fewer large-cap companies that have not already adopted these features, and those companies are often unappealing targets for governance proponents because many have structural hurdles, such as dual class voting, that limit the efficacy of shareholder proposals.

Notwithstanding the continuing decline of governance proposals voted on since 2016 at small- and mid-cap companies, these companies may be experiencing heightened pressure as a consequence of developments in governance proposals and practices. Therefore, over time, the most popular governance practices have become somewhat more common (e.g., destaggered boards) or much more common (e.g., majority voting) at smaller companies, as demonstrated in the following charts:
In recent years, special meeting rights and proxy access also have become more widely adopted, especially among the S&P 500, although they are still comparatively less common. As the following chart illustrates, the number of S&P 500 companies that have adopted special meeting rights has plateaued at around 65%, without much change over the past four years. There is also a significant level of adoption of special meeting rights among large-cap and small-cap companies (around 50% among each of the S&P 400 and S&P 600). This is partially attributable to the fact that many of the smaller companies are incorporated in states that have adopted the Model Business Corporation Act, which mandates the shareholder right to call special meetings (about 30% of S&P 400 companies and 25% of S&P 600 companies are incorporated in states that mandate the right, as compared to about 15% of S&P 500 companies).

Approximately 600 U.S. companies have adopted proxy access provisions at this point, including roughly 73% of the S&P 500. Proxy access was a rarity among public U.S. companies before 2015 but became a favorite topic among shareholder proponents between 2015 and 2017 (the New York City Comptroller was the primary sponsor of these proposals from 2015 to 2017, primarily at large-cap companies). As further discussed in Section E.5 and illustrated in the following chart, in recent years, many large-cap companies have elected to adopt proactively a market standard proxy access provision rather than face a shareholder vote.
1. Independent Chair

<table>
<thead>
<tr>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Voted On</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019 YTD</td>
<td>2018</td>
<td>2019 YTD</td>
<td>2018</td>
</tr>
<tr>
<td>62</td>
<td>54</td>
<td>54</td>
<td>47</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2019 YTD</td>
<td>2018</td>
</tr>
<tr>
<td></td>
<td></td>
<td>29%</td>
<td>32%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

Proposals requesting that the board chair be an independent director were the most common type of governance proposal submitted this year. Large companies have regularly received these proposals since the mid-2000s, and the slight year-over-year increase in the number of proposals on this topic reflects that certain shareholders continue to believe that having the CEO or another executive serve as chair may negatively influence the independence of the board as a whole. Half of the independent chair proposals this year were submitted by John Chevedden, who often referenced recent public controversies to support his call for more robust independent board oversight (for example, at Abbott Laboratories, Anthem and UnitedHealth, Chevedden and his affiliates submitted proposals that cited concerns relating to the opioid crisis in their supporting statements). In connection with the opioid crisis, religious organizations, faith-based coalitions, and their affiliates, including members of ICCR and IOA, also submitted a meaningful number of independent chair proposals at healthcare and pharmaceutical companies, as discussed in Section B. In addition to healthcare and pharmaceutical companies, proponents of independent chairs also focused on tech companies, in part due to the sustained public scrutiny on tech industry corporate culture and human capital management issues, with 12 high profile tech companies (including Amazon, AT&T, Facebook, IBM and Verizon) receiving a proposal on this topic in 2019.

These proposals tend to receive meaningful shareholder support (generally 25% to 40%), but rarely pass. Only a handful each year managed to win majority support between 2012 and 2015, and none passed since.
ISS only recommended in favor of about 39% of proposals (down from about three-quarters in 2018 and more consistent with actual voting results).

2. Board Composition

<table>
<thead>
<tr>
<th>BOARD COMPOSITION</th>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Voted On</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Board diversity</td>
<td>32</td>
<td>27</td>
<td>9</td>
<td>3</td>
</tr>
<tr>
<td>Director qualifications</td>
<td>7</td>
<td>3</td>
<td>0</td>
<td>3</td>
</tr>
</tbody>
</table>

a. Board Diversity

Board diversity, in particular, female representation on boards, has been a topic of continuing and well-publicized focus for lawmakers and regulators:

- Recently, California became the first U.S. state to pass a law setting mandatory thresholds for female directors. On September 30, 2018, California passed Senate Bill 826, which requires publicly held corporations with their principal place of business in California to have at least one woman on their boards by December 31, 2019, with the minimum raised to at least two female directors for companies with five directors and at least three female directors for companies with six or more directors by December 31, 2021.

- Subsequently, lawmakers in other states have taken similar legislative steps. In November 2018, a board gender diversity bill mimicking California Senate Bill 826 was introduced to the New Jersey Assembly, and on February 14, 2019, the bill moved to the Senate as New Jersey Senate Bill No. 3469. On January 11, 2019, a dozen Washington senators introduced Senate Bill 5142, which would apply similar requirements to companies subject to the Washington Business Corporation Act. On January 23, 2019, Illinois Senator Cristina Castro introduced Senate Bill 0076, which would apply to publicly held corporations with their principal place of business in Illinois.

- On February 6, 2019, the Securities and Exchange Commission’s Division of Corporation Finance released Compliance and Disclosure Interpretations (C&DIs) 116.11 and 133.13, which provide that, to the extent a company’s nominating committee considers diversity characteristics such as race, gender, and other self-identified characteristics, the company’s disclosure should include those characteristics and how they were considered.

---

On the same day the SEC released its C&DI s on director diversity disclosures, the “Improving Corporate Governance Through Diversity Act of 2019” was introduced in both houses. The bill seeks to require public companies to disclose the gender, race, ethnicity, and veteran status of their directors and nominees, as well as senior executive officers, and to disclose whether the board has a policy or strategy to promote racial, ethnic, and gender diversity among directors, nominees, and executive officers. The bill has been referred to subcommittees in the House and the Senate for review.

In addition to lawmakers and regulators, companies are also facing pressure from institutional shareholders and proxy advisory firms to increase female representation on their boards:

- State Street Global Advisors (SSGA) stated in its 2019 proxy voting and engagement guidelines that it views board quality as a measure of a variety of factors, including board diversity, and that it expects boards of Russell 3000 and TSX listed companies to include at least one female director.\(^\text{12}\) Since the launch of its “Fearless Girl” campaign in 2017, SSGA has been voting against nominating chairs if there are no female directors on the board, and beginning in 2020, SSGA will vote against the entire nominating committee if there are no female directors on the board.\(^\text{13}\)

- On January 17, 2019, BlackRock released its updated 2019 proxy voting guidelines for U.S. securities. Notable updates include expanding its policy on board diversity to take into account both personal and professional factors and encouraging companies to have at least two women directors on every board.\(^\text{14}\) In February 2018, BlackRock sent letters to all Russell 1000 companies with fewer than two female directors asking the companies to justify how their board diversity aligns with their long-term strategies.

- ISS’s 2019 proxy voting guidelines indicated that for meetings held after February 1, 2020, adverse voting recommendations may be issued against nominating committee chairs of boards of Russell 3000 or S&P 1500 companies with no female directors.\(^\text{15}\)

- Glass Lewis’s Proxy Paper states in its Summary of Changes for the 2019 U.S. Policy Guidelines that per its policy regarding board gender diversity announced in November 2017, for meetings held after January 1, 2019, Glass Lewis will generally recommend against the nominating committee chair of boards with no female members.\(^\text{16}\)

---


A number of social investment entities, governance activists, and other interested parties have formed advocacy groups, most notably the Thirty Percent Coalition, to engage with corporations and the public to advance the cause of board diversity.\textsuperscript{17}

In response to investors’ scrutiny on board diversity, it has become increasingly common for both large- and small-cap companies to address the topic of board gender diversity in their proxy statements. The following chart, which presents the number of proxy statements that include the phrases “women on the board,” “gender diversity” or “female directors,” presents a partial picture of trends in proxy disclosures with respect to board gender diversity.

Female representation on boards has been increasing in recent years, particularly at larger companies. In 2018, approximately 87% of S&P 500 companies had two or more female directors, an increase of 7% from 2017.\textsuperscript{18} Conversely, in 2018, 47% of Russell 3000 companies had boards comprised of less than 15% female members, a decrease of 11% from 2017.\textsuperscript{19}

So far in 2019, shareholders have submitted more board diversity proposals (32) than they did in all of 2018 (27). As was the case in 2018, companies resolved the vast majority of these proposals before they reached a vote, suggesting that companies are continuing to make board gender diversity a priority in

\textsuperscript{17} The name of the Thirty Percent Coalition comes from its goal of having women hold 30% of board seats across public companies. Information about the Coalition is available at https://www.30percentcoalition.org/.


response to many of the above developments, eliminating the perceived need by shareholders to push for a vote on a specific proposal.

Of the nine board diversity proposals that reached a vote in 2019, seven were anti-ESP proposals submitted by the Free Enterprise Project, the conservative shareholder activist arm of the National Center for Public Policy Research (NCPPR). NCPPR seeks to shift companies’ board diversity efforts away from diversity based on race, gender, and other self-identified demographic characteristics, and towards “true board diversity,” defined as a nominee’s skills, experience, and ideological perspectives.

“True board diversity” proposals tend to go to a vote and receive low support. As a result, a larger percentage of board diversity proposals as a whole went to a vote (28% in 2019 compared to 11% in 2018) and voted proposals received lower average shareholder support (8% in 2019 compared to 17% in 2018).

Last year, the NCPPR submitted only one proposal to disclose a “true board diversity” matrix (to Alphabet); ISS recommended against it and the proposal received only 2% of votes cast. ISS recommended against all seven of these proposals this year (to Amazon, Apple, Discovery, Facebook, salesforce.com, Starbucks, and Twitter), and shareholder support remained low at between 1-3% of votes cast.

The other two voted board diversity proposals, which were proposals aimed at increasing board diversity (at Exxon and Skechers), garnered higher shareholder support (at 26.6% and 29.8% of votes cast) and positive ISS recommendations. Adjusting for the true board diversity proposals, both the percentage of voted proposals (8% in 2019 compared to 7.7% in 2018) and the average shareholder support (28% compared to 25% in 2018) were level with 2018.

In light of the current interest in this topic, companies should be prepared to engage with investors on diversity issues and, in particular, to articulate the principles by which the board considers gender, race and other types of diversity in choosing a slate, the steps taken to ensure a diverse pool of potential nominees is considered, and how the board is considering this issue for the upcoming meeting.

---

Exxon sought to exclude the proposal to disclose the skills, qualifications, and diversity of each director in a matrix format, arguing that the director skills matrix they adopted following the receipt of the proposal, which discloses qualifications of the board as a whole, constituted “substantial implementation.” In the SEC’s response on April 2, 2019, the Staff denied relief because Exxon’s board-level matrices “do not provide investors with a means to evaluate an individual nominee’s attributes for the purpose of making informed voting decisions, which appears to be the essential objective of the Proposal.” The proposal went to a vote and received approximately 30% of votes cast.
b. Director Qualifications and Director Tenure

In 2014, the New York City Comptroller launched the Boardroom Accountability Project, a nationwide campaign to implement proxy access. Once that initiative had achieved critical mass, the Boardroom Accountability Project transitioned to its second phase in September 2017, focusing on increasing diversity, independence, and competence on climate-related issues at the board level, especially among larger companies. On September 8, 2017, the Comptroller sent letters to 151 portfolio companies (80% of which are in the S&P 500) asking them to publish standardized annual disclosures on their board qualifications and diversity (including in terms of skills, race, and gender) and board refreshment processes.

The impact of the second phase of the Comptroller’s campaign has been widely felt, as many companies have started to include annual disclosure on board qualifications and diversity in a matrix form. In addition to the board diversity related proposals discussed above, there were seven director qualifications proposals this year, all from the Comptroller requesting more disclosure of director qualifications (many of the board diversity related proposals submitted this year requested disclosure of director qualifications in addition to board diversity; we have not categorized those proposals as director qualification proposals).

Between 2012 and 2018, there have been a few director qualification proposals coming to a vote each year (with eight in 2012 and three in 2018), but none came to a vote in 2019 thus far. No director qualification proposals have passed since 2012. The decline in director qualifications proposals that have been voted on and the large number that have been withdrawn suggest that companies are voluntarily agreeing to make disclosures of director qualifications when these proposals are received.

Another aspect of board composition that is notable for its absence as a proposal topic is director tenure. The topic of director tenure has generated a significant amount of conversation in recent years. A number of investors, investor groups and governance commentators have queried whether there comes a point where a long-tenured director should not be seen as independent and whether mandatory term limits or retirement ages are advisable. For example, in 2014, SSGA announced that it may vote against directors (including the governance committee chair and/or long-tenured members of key committees) when the average board tenure or tenure of individual directors is excessive, which remains part of its voting policy. ISS also added factors on director tenure to its QualityScore ranking in recent years, noting that “excessive tenure is considered to potentially compromise a director’s independence and as such ISS

---

Governance QualityScore will consider the non-executive directors where tenure is higher than the recommended local best practice. 22

However, ISS has not included questions on director tenure in its annual investor survey since 2016, 23 and most institutional investors that set out policies on the topic assess the experience and attributes of the board as a whole and oppose bright-line rules such as age and term limits. BlackRock’s 2019 proxy voting guidelines for U.S. securities state that they are not opposed in principle to long-tenured directors. And, where boards find age or term limits are the most efficient mechanism for ensuring periodic board refreshment, BlackRock defers to the board’s determination in setting those limits. 24

As one component of shareholder engagement, an increasing number of companies now include more meaningful explanations of the manner in which the board considers tenure in assessing board composition and choosing the management slate. The mounting attentiveness of large- and small-cap companies to disclosures on this topic is reflected in the steep rise over the past few years in the number of proxy statements referencing “director tenure” and/or “board refreshment”, as shown in the following chart:

---


3. Shareholder Right to Act by Written Consent

<table>
<thead>
<tr>
<th>SHAREHOLDER PROPOSALS</th>
<th>SHAREHOLDER PROPOSALS</th>
<th>AVERAGE % OF VOTES</th>
<th>SHAREHOLDER PROPOSALS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Submitted</td>
<td>Voted On</td>
<td>Cast in Favor</td>
<td>Passed</td>
</tr>
<tr>
<td>2019 YTD</td>
<td>2018</td>
<td>2019 YTD</td>
<td>2018</td>
</tr>
<tr>
<td>38</td>
<td>41</td>
<td>33</td>
<td>36</td>
</tr>
</tbody>
</table>

There was a significant increase in the number of proposals requesting that the company grant shareholders the right to act by written consent in 2018, reversing a downward trend from 2015 through 2017. In 2019 so far, the number of proposals in this category submitted by shareholders is lower than 2018 but still higher than 2017. The vast majority of these proposals (87%) went to a vote. ISS recommended in favor of about 88% of the written consent proposals voted on in 2019, and the proposals, as usual, received relatively strong support levels. In 2019, six proposals (18% of the total voted on) have passed so far, the same as in all of 2018, although there was a slight decline in the level of overall support for these proposals.

The corporate laws of most states provide that shareholders may act by written consent in lieu of a meeting unless the company’s certificate of incorporation provides otherwise. Commonly, public companies provide in their charters that shareholders may not act by written consent, or that they may act by written consent only if the consent is unanimous. The main concern that companies have about giving shareholders the right to act by written consent is that the written consent process can frustrate the orderly and transparent debate on the merits that would occur if the proposed action were raised at a shareholder meeting.

In 2019, all but one company that had written consent proposals up for a vote already provided shareholders with the right to call a special meeting. All of these companies stressed in their opposition statements that adopting a written consent provision would be unnecessary, and potentially detrimental to shareholder interests, in light of existing corporate governance structures and practices. The relatively low
SULLIVAN & CROMWELL LLP

success rate of written consent proposals in both 2019 and 2018 seems to reflect continuing agreement by a majority of shareholders that special meeting rights adequately address this concern and render written consent rights unnecessary. When companies do implement a written consent right today, the right is often subject to a number of the same terms contained in market standard special meeting provisions, such as defined waiting periods, disclosure requirements (including disclosures to shareholders who are not solicited), holding requirements, and black-outs, as further discussed in Section E.6.

4. Elimination of Supermajority Thresholds, Majority Voting in Uncontested Elections and Board Declassification

<table>
<thead>
<tr>
<th>MOST SUCCESSFUL GOVERNANCE PROPOSALS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shareholder Proposals Submitted</td>
</tr>
<tr>
<td>Eliminate Supermajority Thresholds</td>
</tr>
<tr>
<td>Majority Voting in Uncontested Elections</td>
</tr>
<tr>
<td>Declassify Board</td>
</tr>
</tbody>
</table>

In previous years, the only shareholder proposals that passed on a consistent basis have been the three governance proposals that have been widely adopted at large companies – elimination of supermajority voting thresholds to effect certain corporate actions (such as charter or bylaw changes or the removal of directors), majority voting in uncontested director elections (rather than plurality voting), and declassification of boards. Although these three types of governance proposals still managed to pass this year at almost every company where they reached a vote, only proposals relating to elimination of supermajority voting thresholds reached a vote a meaningful number of times (19, compared to seven majority voting proposals and four declassification of board proposals).

Around 36% of the proposals on these topics have been at non-S&P 500 companies this year. As shown in the charts at the beginning of this Section, these governance reforms are common among large-cap companies, and have been steadily advancing at smaller companies as well (particularly majority voting). The widespread adoption of these practices has led to a sharp decrease in these proposals in recent years at both large- and small-cap companies. Approximately 90% of S&P 500 companies and 47% of Russell 3000 companies have adopted some form of majority voting in uncontested director elections. Additionally, the practice of requiring supermajority votes has also declined, with only 38.8% of the S&P 500 requiring a supermajority vote for changing the charter and 24.1% requiring a supermajority vote for changing bylaws in 2019.
5. Proxy Access Proposals

<table>
<thead>
<tr>
<th>PROXY ACCESS</th>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Voted On</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adopt new right</td>
<td>11</td>
<td>18</td>
<td>5</td>
<td>10</td>
</tr>
<tr>
<td>Amend existing right</td>
<td>22</td>
<td>29</td>
<td>22</td>
<td>25</td>
</tr>
</tbody>
</table>

This year saw a further decrease in the number of proxy access proposals voted on, continuing the trend in 2018. As discussed in the beginning of this Section, almost 600 companies have adopted proxy access rights, including roughly 73% of S&P 500 companies and 19% of Russell 3000 companies. Given the widespread and continued adoption of proxy access bylaws at larger companies, it is unsurprising that shareholders submitted fewer proposals for the adoption of a new proxy access right this year.

Over the past four years, there has been significant convergence in the terms of proxy access provisions adopted by companies, with the market standard now being a so-called 3/3/20/20 bylaw—that is, a threshold of 3% ownership for three years, a director cap of 20% of the board but no less than two, and a group limit of 20 shareholders. Continuing a trend that began in 2017, most companies receiving a proposal to adopt proxy access opted to adopt the market-standard bylaw before a vote, resulting in a near elimination of such proposals that reached a shareholder meeting in 2019 (five total, compared to ten in 2018 and 28 in 2017). The pass rate of these proposals was higher in 2019 (60%) compared to 2018 (30%). Of the two proposals that did not receive majority support, one appears to have failed due to idiosyncratic reasons.25

As more companies implement proxy access, some have expected to see a rise in shareholder proposals to amend existing proxy access rights. However, the number submitted this year so far decreased by 24% (22 in 2019, compared to 29 in all of 2018). All of the submitted proposals reached a vote in 2019, compared to 86% in 2018. As was the case in the past two years, none of these proposals passed. These proposals did receive meaningful average support from shareholders (29% in 2019, 28% in 2018 and 2017), and ISS supported all of them. They generally sought to remove limits on the size of shareholder groups, and/or to remove various other limitations on the use of proxy access, like the percentage vote required to qualify a shareholder proxy access director candidate.

In appropriate cases, Rule 14a-8(i)(10) is available to exclude shareholder proposals to adopt or amend a proxy access bylaw as “substantially implemented.” Throughout 2016, 2017, and 2018, the SEC generally allowed the exclusion of shareholder proposals for a new proxy access right if a company adopts a

---

25 The New York City Comptroller’s proposal to vote for a change to Universal Health Services’ bylaws to adopt proxy access was unlikely to pass because it needed support from the company’s CEO, who controls 83.6% of total voting power.
3/3/2020 provision, even if the company’s bylaw contains terms that are different from the shareholder’s proposal (for example, imposing a lower group size limit, so long as the ownership percentage and duration thresholds matched those proposed by the shareholder) or imposes additional requirements on proxy access (such as a “net long” definition of ownership or qualification requirements for nominees). With respect to proposals to amend a proxy access bylaw, the SEC denied no-action relief to each of the two requests for relief in 2019.

6. Shareholder Right to Call Special Meetings

<table>
<thead>
<tr>
<th></th>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Voted On</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adopt New Right</td>
<td>1</td>
<td>18</td>
<td>1</td>
<td>8</td>
</tr>
<tr>
<td>Lower % on Existing Rights</td>
<td>25</td>
<td>59</td>
<td>20</td>
<td>53</td>
</tr>
</tbody>
</table>

Proxy advisory firms and many shareholders support the right of shareholders to call a special meeting, because it enables shareholders to act on matters that arise between annual meetings (such as the replacement of one or more directors, including in circumstances intended to permit an acquisition offer to proceed, or the amendment of bylaws). The right to call special meetings should be viewed in conjunction with the strong movement away from classified boards—in Delaware, directors of a non-classified board can generally be removed by shareholders without cause. Thus, given the trend of declassifying boards, the ability to act outside the annual meeting to remove directors without cause and elect their replacements can be viewed as the dismantling of an effective mechanism to provide directors with additional time to respond to shareholder activism or consider hostile takeover proposals. Nearly two-thirds of S&P 500 companies (about the same level as last year) now provide shareholders with some right to call a special meeting, a development driven largely by shareholder proposals and shareholder support for the concept over the past decade. Consequently, this type of proposal is no longer the most frequently proposed.

a. Types of Proposals

Only one company received a shareholder proposal to add a special meeting right so far this year. Although the proposal received ISS support, it ultimately did not pass, receiving only 42% shareholder support.

Last year, proposals seeking to reduce the ownership threshold to call a special meeting were the most common type of governance-related proposal, and there have been 25 proposals to reduce special meeting thresholds in 2019 so far, compared to 59 submitted in all of 2018. The vast majority of these proposals (80%) went to a vote. Most of these proposals were submitted by John Chevedden or Kenneth Steiner.
Of the 20 reduce special meeting threshold proposals that came to a vote in 2019, 16 sought to reduce a 20% or 25% threshold to either 10% or 15%. These proposals continued to receive high shareholder support this year (averaging 44% in 2019 compared to 40% in 2018), with four managing to gain majority support, the same as in 2018. The significant level of support these proposals continue to receive suggests that some governance-focused shareholders are not satisfied with the 25% ownership threshold that has become the market standard at large companies.

b. Terms to Consider When Adopting or Amending a Special Meeting Provision

Companies putting forth a new special meeting right or evaluating an existing right, either preemptively or in response to a proposal, may wish to consider the following terms:

- **Threshold.** Though practice varies, for a number of years 25% has been the most common threshold for special meeting rights at public companies, as reflected in the following chart showing the threshold for special meeting rights at Delaware companies among the S&P 500.\(^{26}\) BlackRock’s current policies indicate that it generally believes a threshold between 15–25% is reasonable “in order to avoid the waste of corporate resources in addressing narrowly supported interests.”\(^{27}\) They also believe that a right to act by written consent is “not a sufficient alternative to the right to call a special meeting.”\(^{28}\) However, companies with a 25% threshold should monitor and consider developments at peer companies on special meeting proposals and practices. Although some large institutional investors may continue to support a 25% threshold, the meaningful shareholder support for proposals to move from a 25% to a 10–15% threshold indicates that a substantial portion of a company’s other shareholders may support making special meeting rights more accessible.

---

\(^{26}\) Based on data from FactSet Shark Repellent. We have limited this analysis to Delaware companies, because certain other states provide a statutory default special meeting right at 10%.


• **Definition of ownership.** Many companies require “record” ownership of shares (as opposed to “beneficial” ownership), essentially requiring street name holders to work through their securities intermediaries to become a record holder. This eliminates uncertainty as to proof of ownership, but introduces an additional administrative step for shareholders seeking to use the right. In addition, a number of companies have introduced a “net long ownership” concept into their special meeting provision—essentially reducing the shareholders’ actual ownership level by any short positions or other hedging of economic exposure to the shares. Companies that do not include a “net long” concept should nevertheless provide that the information required from the requesting shareholders must include details of any hedging transactions, so that the company and other shareholders can have a full picture of the requesting shareholders’ economic stake in the company.

• **Pre- and post-meeting blackout periods.** In order to avoid duplicative or unnecessary meetings, many companies provide that no meeting request will be valid if it is received during a specified period (usually 90 days) before the annual meeting, or during a specified period (usually 90 or 120 days) after a meeting at which a similar matter was on the agenda.

• **Limitations of matters covered.** Special meeting provisions typically provide that the special meeting request must specify the matter to be voted on, and that no meeting will be called if, among other things, the matter is not a proper subject for shareholder action. Generally, the only items that may be raised at the special meeting will be the items specified in the meeting request and any other matters that the board determines to include.

• **Timing of meeting.** Companies typically provide that the board must set the meeting for a date within 90 days from the receipt of a valid request by the requisite percentage of shareholders. Often, the special meeting provisions provide that, in lieu of calling a special meeting, the company may include the specified item in a meeting called by the company within that same time period.

• **Holding period.** A few companies require the requesting shareholders to have held the requisite number of shares for a specified period of time prior to the request.

• **Inclusion in charter versus bylaws.** Companies should consider whether to include the special meeting provisions in the charter, the bylaws or a combination. In some cases, companies include the critical provisions (such as ownership threshold) in the charter so that shareholders cannot unilaterally amend them, but provide the details and mechanics in the bylaws, so that they can be adjusted by the board without a shareholder vote.
7. Dual Class Voting

<table>
<thead>
<tr>
<th>Shareholder Proposals</th>
<th>Shareholder Proposals</th>
<th>Average % of Votes</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td>7</td>
<td>11</td>
<td>6</td>
<td>10</td>
</tr>
</tbody>
</table>

Over the years, dual class voting has ranked among the most controversial topics in corporate governance, and the debate continued to be animated during the last 12 months. On March 14, 2019, a group of institutional investors with $3.2 trillion assets under management issued a letter urging Lyft’s board of directors to adopt the one share, one vote structure or to adopt a near-term sunset provision for its dual class structure. In October 2018, the Council of Institutional Investors, backed by BlackRock and T. Rowe Price Group, filed petitions with the New York Stock Exchange and the NASDAQ, calling on them to limit listings of companies with dual class share structures. The prevalence of the dual class structure is in part due to its widespread use by technology companies, with nearly 50% of recent technology listings having a dual class status.

However, proposals to eliminate supervoting stock (either by adopting a recapitalization plan for all equity securities to have one vote per share or by converting the supervoting shares into low-vote shares) are typically among the least common types of governance-related proposals each year. Six such proposals came to a vote in 2019 so far, compared to 10 in all of 2018. These proposals received about the same level of shareholder support in 2019 (average support of 27%) as in 2018 (average support of 32%). Despite ISS’s support for all of these proposals, none of them passed, which is not surprising when the holders of supervoting stock vote against them.

Proposals to reclassify supervoting shares do not reflect the full extent of the impact of the debate on dual class voting. For example, the increased scrutiny on dual class companies may translate into negative votes for directors. ISS’s 2018 policy updates specifically provide for a negative director vote recommendation at newly public companies where the classes have unequal voting rights, as we will discuss in Part 2 of our 2019 proxy season review. Glass Lewis indicated in its 2019 Proxy Paper that in evaluating dual class companies’ board responsiveness in 2019, it will consider the level of approval or disapproval attributed to unaffiliated shareholders. It expects that where vote results indicate a majority of

---


unaffiliated shareholders voted in support of or against a proposal, the board should demonstrate an appropriate level of responsiveness.

In addition, some stakeholders have resorted to means outside of shareholder proposals to generate momentum for change at dual class companies. For instance, the NYC Comptroller recently released a letter announcing it will no longer vote in favor of Facebook, to draw attention to a perceived lack of accountability contributing to mismanagement of public incidents. Employees of Alphabet staged a global walk-out to protest the company’s handling of sexual harassment, which shareholders cited as support for a proposal requesting the company to reform its policies on sexual harassment and executive exit packages.

8. Other Governance Proposals

Some less frequent and less successful governance-related proposals are addressed below:

- **No Abstentions in Vote Counting.** The past few years have seen a number of proposals asking that the general standard for shareholder action be “majority of votes cast” rather than the common standard, and Delaware default, of “majority of votes present at the meeting in person or by proxy and entitled to vote.” The only difference is that, in the latter case, the denominator includes abstentions, as well as “for” and “against” votes. Such a change would have little practical impact, as most shareholder proposals are precatory anyway, so the legal standard for passing is irrelevant. In addition, the number of abstentions (not to be confused with broker non-votes, which is where a broker is not entitled to vote, and so excluded from both standards) is generally small. Only one of these proposals came to a vote in 2019 and in 2018, compared to 10 in 2017. The lack of practical impact likely explains both the low frequency and low vote results for these proposals, which received an average of less than 10% support in 2017 through 2019. No proposal in either year came close to passing.

- **Mandatory Arbitration Bylaw Provisions.** The issue of mandatory arbitration provisions in the bylaws of U.S. publicly listed companies has recently become a highly controversial issue. Chairman Clayton of the SEC issued a public statement on February 11, 2019 backing a no-action letter sent to Johnson & Johnson Co. that allowed it to omit a shareholder proposal on mandatory arbitration from its proxy but emphasizing that views expressed in no-action letters are not binding, and “[a] court is a more appropriate venue to seek a binding determination of whether a shareholder proposal can be excluded.” The proposal sought to have the board adopt mandatory arbitration of shareholder claims, but was excluded on the basis that such action violated both state and federal law, making it invalid for a shareholder vote. Notably, the shareholder that submitted this proposal acted on Chairman Clayton’s recommendation and commenced a lawsuit in the District of New Jersey alleging, among other things, that Johnson & Johnson Co. violated federal securities law by improperly excluding the shareholder proposal from its proxy. While this lawsuit is still in its infancy, CalPERS and Colorado PERS have both intervened in the lawsuit, potentially teeing up a decision with large corporate governance ramifications. If the court were to find that mandatory board arbitration did not violate federal and state law (and thus the proposal was improperly excluded), companies will begin to see a proliferation of proposals for and against mandatory board arbitration.

---

• **Virtual-Only Meetings.** Over the last three years, an increasing number of companies have moved from in-person meetings to virtual-only meetings. However, based on a 2018 ISS survey, 8% of institutional investors did not support either virtual-only or “hybrid” (both physical and electronic/online) meetings, and 36% considered hybrid shareholder meetings to be acceptable but not virtual-only meetings. In addition, effective in 2019, Glass Lewis’s policy is to vote against governance committee members at companies without in-person meetings unless their proxy materials contain disclosures that are sufficiently robust to assure shareholders that they would not lose any participation rights by moving to virtual-only meetings. Earlier this year, Frontier Communications received a shareholder proposal to hold a face-to-face annual meeting with shareholders starting in 2020 (Frontier Communications held a virtual meeting in 2019). The SEC staff granted no-action relief to Frontier Communications, agreeing with the company that this proposal related to ordinary business operations. This was the only shareholder proposal related to virtual meetings this season, and therefore it is too early to predict whether the Staff will continue to permit such proposals to be excluded.
F. COMPENSATION-RELATED SHAREHOLDER PROPOSALS

<table>
<thead>
<tr>
<th>COMPENSATION-RELATED PROPOSALS</th>
<th>Shareholder Proposals Submitted</th>
<th>Shareholder Proposals Voted On</th>
<th>Average % of Votes Cast in Favor</th>
<th>Shareholder Proposals Passed</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2019 YTD</td>
<td>2018</td>
<td>2019 YTD</td>
<td>2018</td>
</tr>
<tr>
<td>Social compensation issues</td>
<td>18</td>
<td>24</td>
<td>9</td>
<td>14</td>
</tr>
<tr>
<td>Limit golden parachutes</td>
<td>1</td>
<td>7</td>
<td>0</td>
<td>7</td>
</tr>
<tr>
<td>Clawbacks</td>
<td>8</td>
<td>11</td>
<td>5</td>
<td>7</td>
</tr>
<tr>
<td>Stock retention</td>
<td>2</td>
<td>2</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Compensation – other</td>
<td>23</td>
<td>22</td>
<td>15</td>
<td>13</td>
</tr>
</tbody>
</table>

From 2012 to 2017, there was a steep decline in the number of compensation-related proposals, in large part a result of mandatory say-on-pay votes becoming the primary mechanism by which shareholders express concerns over executive compensation. In 2018, the number of compensation-related proposals leveled out, and this trend has continued in 2019. Compensation-related proposals still tended to receive relatively low support, although two passed this year.

The most common type of compensation-related proposal in 2019 sought to link executive compensation to social issues, such as sustainability or social or environmental impact. Though there have been fewer ESP compensation-related proposals so far in 2019, the number was still higher than 2017 (12 submitted). Shareholder proposals linking compensation to ESP issues may increase going forward; for example, Trillium Asset Management has hinted that it is contemplating submitting proposals linking diversity performance metrics to senior executive compensation, as discussed in Section D.3.b. Similar to 2018, half of these proposals reached a vote in 2019 (nine total, including five proposals relating to the integration of drug pricing risks into compensation plans at pharmaceutical companies).33 Five of the compensation proposals relating to social issues that did not go to a vote were withdrawn (covering drug pricing risks, greenhouse gas reduction and human rights risks), while the other three (two covering sustainability as a performance measure) were excluded.

ISS supported 70% of the compensation-related proposals voted on so far in 2019, and shareholder support averaged 31% for proposals where ISS recommended in favor, as compared to 9% for proposals where ISS recommended against. ISS recommended in favor of all clawback-related proposals, continuing the trend from 2018, which likely is also responsible for the continued increase in average support for this proposal in 2019. One of the two clawback-related proposals that passed this year was at drug maker Mallinckrodt, who also had a lobbying proposal pass this year, as discussed in Section D. The other was at FleetCor Technologies.

---

33 These included AbbVie, Johnson & Johnson, Merck, Pfizer, and Vertex.
Proposals to limit golden parachutes (i.e., acceleration of performance awards upon a change in control) and to enhance executive stock retention requirements saw temporary increases in frequency and support levels in 2014 and 2015, but have since slowed to a trickle.

This year, two proposals on data privacy and cybersecurity as performance metrics for senior executive compensation went to a vote. ISS supported the proposal submitted to Walt Disney, although it received only 26.8% shareholder support. Recent regulatory changes, such as recent SEC cybersecurity guidance and new data privacy laws (e.g., the General Data Protection Regulation in the E.U.), may spur shareholders to submit more proposals of this type going forward, in particular if they consider a company’s disclosures on issues relating to cybersecurity and/or data privacy to be outdated, overly generalized or otherwise lacking. The SEC issued guidance on cybersecurity disclosures in February 2018 and issued an Investigative Report in October 2018 urging public companies to consider cyber threats when implementing internal accounting controls, based on its investigations of nine public companies that were victim to cyber fraud. In connection with these regulatory developments, it has become increasingly common for both large- and small-cap companies to address the topic of cybersecurity in their proxy statements. The number of proxy statements that included the term “cyber,” which presents a partial picture of trends in proxy disclosures with respect to cybersecurity risk oversight, has risen steadily:

![Proxy Statements Including Term “Cyber”](image)

34 Walt Disney and Verizon received requests to assess the feasibility of using cybersecurity and data privacy as performance measures for senior executive compensation. The proposals went to a vote on March 7, 2019 and May 2, 2019, respectively.


2019 Proxy Season Review
Part 1 – Rule 14a-8 Shareholder Proposals
Notwithstanding the trend of proactive disclosure on cybersecurity, given the recent attention on this subject, shareholder proposals on cybersecurity issues may increase going forward. One future source of shareholder movement may relate to companies and their handling of facial recognition technology. This year, Amazon received two proposals related to facial recognition – one to prohibit the sale of facial recognition technology to government agencies unless it is found to not harm civil and human rights, the other to report on the impact of government use of its facial recognition technology. As facial recognition becomes more prevalent in fraud prevention and security, companies may expect increased disclosure regarding their use of this technology and data.
G. NO-ACTION RELIEF

Through June 30, 84 S&P Composite 1500 companies challenged a total of 156 proposals through the SEC no-action process, amounting to almost 25% of all proposals submitted. Around 46% of these challenged proposals were governance-related, 41% were ESP-related and 13% were compensation-related. Out of these no-action requests, the SEC staff granted full relief to 108 (or 69%), partial relief to three (or 2%), and denied the remaining 45 (or 29%). The vast majority of the 45 proposals where relief was denied went to a vote, with only three withdrawn.

Of the proposals subject to no-action requests, the most popular ones were environmental (15% of all no-action requests), eliminating supermajority voting (9%), and requiring independent board chairman (6%). Proposals that companies are most likely to challenge through the no-action process include declassify-the-board proposals (83% of all declassify-the-board proposals were challenged) and animal rights proposals (71%). Of the 111 no-action requests that received full or partial relief from the SEC, over 50% were governance-related proposals, closely followed by ESP proposals (40%). The most successfully excluded proposals were reduce special meeting threshold proposals (100% success rate), animal rights (100%), human rights (83%), and eliminate supermajority voting (79%).

The landscape for no-action relief is constantly changing as the SEC staff refines its criteria for granting relief. Although the changes have not been as dramatic as some predicted at the beginning of this season, companies should take these changes into account as they evaluate potential avenues for exclusion with respect to the shareholder proposals they receive for the 2020 season.

1. Ordinary Business

Companies seeking to exclude ESP proposals rely heavily on 14a-8(i)(7), the “ordinary business” exception. Last year, the SEC staff set a precedent for providing no-action relief under the micromanagement prong of 14a-8(i)(7) when it agreed with EOG Resources that a shareholder proposal asking the company to adopt “quantitative, time-bound targets for reducing greenhouse gas (GHG) emissions,” and to issue a report “discussing its plans and progress towards achieving these targets,” sought to micromanage the company. Notably, this year the SEC staff provided no-action relief to Devon Energy and Exxon, allowing the companies to exclude proposals from the George Gund Foundation and the New York State Common Retirement Fund, each seeking annual reporting that would include disclosure of greenhouse gas reduction targets aligned with the Paris Climate Agreement. In each case, the SEC staff determined the proposal would “micromanage the company by seeking to impose specific methods for implementing complex policies in place of the ongoing judgments of management as overseen by its board of directors.”

The SEC staff, however, did not agree with Anadarko Petroleum that a shareholder proposal from Jeanne Miller requesting that the company issue a report “describing if, and how, it plans to reduce its total contribution to climate change,” and align its investments and operations with the goals of the Paris
Climate Agreement, sought to micromanage the company, and instead found that the proposal transcends ordinary business matters. This is consistent with the SEC’s responses to other no-action requests on other types of ESP proposals, including proposals related to the allocation of tax savings, immigration detention and mandatory employee arbitration. Nearly two-thirds of climate-related proposals filed with publicly held energy and utility companies have been challenged. The SEC has provided no-action relief to 45% of these proposals, the highest percentage in the last five years. Notably, the proponent behind the climate-related shareholder proposal challenged by Anadarko “took the opportunity to raise a big red flag about recent trends with regard to expanded interpretations of Rule 14a-8(i)(7),”37 highlighting the numerous no-action requests in the 2019 season aimed at excluding shareholder proposals dealing with “long-standing and established areas of shareholder concern,” such as “management of greenhouse gases, the use of antibiotics in the supply chain, promotion of gender equity management of the firm’s pollution impacts, [and] impacts on civil rights.”

Before the 2019 proxy season, the SEC staff continued to refine the “ordinary business” exclusion. In October 2018, the staff of the SEC’s Division of Corporation Finance issued Staff Legal Bulletin No. 14J (“SLB 14J”), which provided guidance on the excludability of shareholder proposals on the basis that they seek to “micromanage” the company. The Staff clarified that under the “ordinary business” exception, a company may exclude a shareholder proposal for micromanaging if it “involves intricate detail, or seeks to impose specific time-frames or methods for implementing complex policies.”38 The SEC staff noted that even if the underlying subject matter is appropriate, a shareholder proposal may still be excluded for micromanagement. The Staff in SLB 14J also clarified that companies may exclude proposals styled as addressing senior executive and/or director compensation but that have as their underlying concern ordinary business matters. The guidance also clarified that proposals addressing senior executive and/or director compensation also may be excludable if a primary aspect of the targeted compensation is broadly available or applicable to a company’s general workforce. Finally, SLB 14J continued to encourage companies to include their boards’ analyses in no-action requests arguing “ordinary business” or “economic relevance.” (Rule 14a-8(i)(5).) The new guidance explained that the most helpful analyses from the 2018 proxy season focused on the specific substantive factors the board considered to arrive at its conclusion that an issue is not sufficiently significant in relation to its business (in the case of “ordinary business”) or not sufficiently significant (in instances of “economic relevance”). The guidance notes that the existence or absence of a discussion of the board’s analysis will not create a presumption either against or for exclusion. Despite SLB 14J, the number of successful challenges to shareholder proposals


that included board analysis has been limited and the SEC staff appears to be reticent to grant no-action relief on board analysis alone.

2. Substantial Implementation

In certain cases, Rule 14a-8(i)(10) is available to exclude shareholder proposals as “substantially implemented.” Historically, this rule has been used to exclude shareholder proposals on proxy access. Throughout 2016, 2017, and 2018, the SEC staff generally allowed the exclusion of shareholder proposals for a new proxy access right if a company adopts a 3/3/20/20 provision, even if the company’s bylaw contains terms that are different from the shareholder’s proposal (for example, imposing a lower group size limit, so long as the ownership percentage and duration thresholds matched those proposed by the shareholder) or imposes additional requirements on proxy access (such as a “net long” definition of ownership or qualification requirements for nominees). With respect to proposals to amend a proxy access bylaw, the SEC staff denied no-action relief to each of the two requests for relief in 2019.

3. Conflicting Management Proposals

On the basis of a conflicting management proposal, companies often seek no-action relief under Rule 14a-8(i)(9). The SEC staff granted no-action relief to Franklin Resources under Rule 14a-8(i)(9), allowing the company to exclude a proposal from James McRitchie and John Chevedden seeking a reduction of the existing ownership threshold for special meetings from 25% to 15% because the proposal conflicted with a management proposal to ratify the current ownership threshold. Notably, the SEC denied Leidos’s challenge to a shareholder proposal from Kenneth Steiner and John Chevedden seeking to reduce the company’s supermajority vote requirement. The SEC was unable to concur with Leidos in its view that the proposal would directly conflict with the company’s own proposal because both proposals sought to reduce the supermajority voting requirements and a reasonable shareholder could logically vote in favor of both.39 This shareholder proposal went to a vote and passed with overwhelming support, with 92.1% of the votes in favor of the proposal.

Companies should consider ISS’s and Glass Lewis’s potential responses when deciding whether to exclude shareholder proposals under Rule 14a-8(i)(9). In its 2019 policy update, ISS codified a new policy regarding conflicting management proposals. ISS will now recommend against individual directors, members of the governance committee, or the full board where the board asks shareholders to ratify existing charter or bylaw provisions. ISS will consider the following:

- The presence of a shareholder proposal addressing the same issue on the same ballot;

---

The board's rationale for seeking ratification;
Disclosure of actions to be taken by the board should the ratification proposal fail;
Disclosure of shareholder engagement regarding the board’s ratification request;
The level of impairment to shareholders' rights caused by the existing provision;
The history of management and shareholder proposals on the provision at the company's past meetings;
Whether the current provision was adopted in response to the shareholder proposal;
The company's ownership structure; and
Previous use of ratification proposals to exclude shareholder proposals.

In announcing this new proposal, ISS specifically noted the frequent use of no-action requests to exclude similar shareholder proposals as "conflicting."

In its 2019 proxy advice guidelines, Glass Lewis has adopted a similar, case-by-case approach with respect to companies that have excluded shareholder proposals as a result of conflicting management proposals, and may recommend against the chair or members of the governance committee. Glass Lewis will consider the following:

- The nature of the underlying issue;
- The benefit to shareholders of implementing the proposal;
- The materiality of the differences between the terms of the shareholder proposal and management proposal;
- The context of a company’s shareholder base, corporate structure and other relevant circumstances; and
- A company’s overall governance profile and, specifically, its responsiveness to shareholders as evidenced by a company’s response to previous shareholder proposals and its adoption of progressive shareholder rights provisions.

According to the 2019 guidelines, Glass Lewis finds Rule 14a-8(i)(9) exclusions especially problematic when a shareholder proposal to reduce special-meeting thresholds is excluded as conflicting with management’s proposal to ratify the existing provision or a provision that is materially different from the shareholder proposal. In those cases, Glass Lewis will generally recommend voting against the chairs or members of the governance committee.

---

H. EXEMPT SOLICITATIONS

Each year, some institutional shareholders (including public pension funds) file notices of exempt solicitation with the SEC under Rule 14a-6(g) to encourage votes on shareholder proposals, say-on-pay proposals and in “vote no” campaigns. Rule 14a-6(g) requires a person who conducts a solicitation of shareholders that is exempt (because the person does not seek to have proxies granted) and who owns more than $5 million of the company’s securities to file with the SEC all written materials used. These notices of exempt solicitation appear on the SEC’s Edgar internet system as “PX14A6G” filings.

Last fall, the SEC staff published two C&DIs regarding PX14A6G filings. C&DI 126.06 clarified that the staff will not object to a voluntary submission of PX14A6G filing, while requiring the cover notice to clearly state that such filing is being submitted on a voluntary basis. C&DI 126.07 specifies how such information should be presented when making a PX14A6G filing.

So far in 2019, 170 PX14A6G filings have been submitted to the SEC, representing a 21% increase from the 140 submitted last year at this time. Of these 170, 39 have been filed voluntarily by some of the most prominent shareholder proponents, including John Chevedden. Many of these voluntary submissions consist solely of “tweets” or other social media posts, while other proponents are filing press releases.
SULLIVAN & CROMWELL LLP

ABOUT SULLIVAN & CROMWELL LLP
Sullivan & Cromwell LLP is a global law firm that advises on major domestic and cross-border M&A, finance, corporate and real estate transactions, significant litigation and corporate investigations, and complex restructuring, regulatory, tax and estate planning matters. Founded in 1879, Sullivan & Cromwell LLP has more than 875 lawyers on four continents, with four offices in the United States, including its headquarters in New York, four offices in Europe, two in Australia and three in Asia.

CONTACTING SULLIVAN & CROMWELL LLP
This publication is provided by Sullivan & Cromwell LLP as a service to clients and colleagues. The information contained in this publication should not be construed as legal advice. Questions regarding the matters discussed in this publication may be directed to any of our lawyers listed below, or to any other Sullivan & Cromwell LLP lawyer with whom you have consulted in the past on similar matters. If you have not received this publication directly from us, you may obtain a copy of any past or future publications by sending an e-mail to SCPublications@sullcrom.com.

CONTACTS

<table>
<thead>
<tr>
<th>New York</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Frank J. Aquila</td>
<td>+1-212-558-4048</td>
<td><a href="mailto:aquilaf@sullcrom.com">aquilaf@sullcrom.com</a></td>
</tr>
<tr>
<td>Robert E. Buckholz</td>
<td>+1-212-558-3876</td>
<td><a href="mailto:buckholzr@sullcrom.com">buckholzr@sullcrom.com</a></td>
</tr>
<tr>
<td>Catherine M. Clarkin</td>
<td>+1-212-558-4175</td>
<td><a href="mailto:clarkinc@sullcrom.com">clarkinc@sullcrom.com</a></td>
</tr>
<tr>
<td>Audra D. Cohen</td>
<td>+1-212-558-3275</td>
<td><a href="mailto:cohen@sullcrom.com">cohen@sullcrom.com</a></td>
</tr>
<tr>
<td>H. Rodgin Cohen</td>
<td>+1-212-558-3534</td>
<td><a href="mailto:cohenhr@sullcrom.com">cohenhr@sullcrom.com</a></td>
</tr>
<tr>
<td>Heather L. Coleman</td>
<td>+1-212-558-4600</td>
<td><a href="mailto:colemanh@sullcrom.com">colemanh@sullcrom.com</a></td>
</tr>
<tr>
<td>Robert W. Downes</td>
<td>+1-212-558-4312</td>
<td><a href="mailto:downesr@sullcrom.com">downesr@sullcrom.com</a></td>
</tr>
<tr>
<td>Mitchell S. Eitel</td>
<td>+1-212-558-4960</td>
<td><a href="mailto:eitel@sullcrom.com">eitel@sullcrom.com</a></td>
</tr>
<tr>
<td>William G. Farrar</td>
<td>+1-212-558-4940</td>
<td><a href="mailto:farrarw@sullcrom.com">farrarw@sullcrom.com</a></td>
</tr>
<tr>
<td>Matthew M. Friestedt</td>
<td>+1-212-558-3370</td>
<td><a href="mailto:friestedtm@sullcrom.com">friestedtm@sullcrom.com</a></td>
</tr>
<tr>
<td>Joseph B. Frumkin</td>
<td>+1-212-558-4101</td>
<td><a href="mailto:frumkinj@sullcrom.com">frumkinj@sullcrom.com</a></td>
</tr>
<tr>
<td>Scott D. Miller</td>
<td>+1-212-558-3109</td>
<td><a href="mailto:millersc@sullcrom.com">millersc@sullcrom.com</a></td>
</tr>
<tr>
<td>Robert W. Reeder III</td>
<td>+1-212-558-3755</td>
<td><a href="mailto:reederr@sullcrom.com">reederr@sullcrom.com</a></td>
</tr>
<tr>
<td>Melissa Sawyer</td>
<td>+1-212-558-4243</td>
<td><a href="mailto:sawyerm@sullcrom.com">sawyerm@sullcrom.com</a></td>
</tr>
<tr>
<td>William D. Torchiana</td>
<td>+1-212-558-4056</td>
<td><a href="mailto:torchianaw@sullcrom.com">torchianaw@sullcrom.com</a></td>
</tr>
<tr>
<td>Marc Trevino</td>
<td>+1-212-558-4239</td>
<td><a href="mailto:trevinom@sullcrom.com">trevinom@sullcrom.com</a></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Los Angeles</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Patrick S. Brown</td>
<td>+1-310-712-6603</td>
<td><a href="mailto:brownp@sullcrom.com">brownp@sullcrom.com</a></td>
</tr>
<tr>
<td>Eric M. Krautheimer</td>
<td>+1-310-712-6678</td>
<td><a href="mailto:krautheimere@sullcrom.com">krautheimere@sullcrom.com</a></td>
</tr>
<tr>
<td>Alison S. Ressler</td>
<td>+1-310-712-6630</td>
<td><a href="mailto:resslera@sullcrom.com">resslera@sullcrom.com</a></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Palo Alto</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Sarah P. Payne</td>
<td>+1-650-461-5669</td>
<td><a href="mailto:paynesa@sullcrom.com">paynesa@sullcrom.com</a></td>
</tr>
</tbody>
</table>
London
Jonathan Horsfield-Bradbury  +44-20-7959-8491 horsfieldbradburyj@sullcrom.com
Jeremy B. Kutner  +44-20-7959-8484 kulnerj@sullcrom.com
Evan S. Simpson  +44 20 7959 8426 simpson@sullcrom.com

Paris
Olivier de Vilmorin  +33-1-7304-1000 devilmorino@sullcrom.com
William D. Torchiana  +33-1-7304-5890 torchianaw@sullcrom.com

Frankfurt
Carsten Berrar  +49-69-4272-5506 berrarc@sullcrom.com
Krystian Czerniecki  +49-69-4272-5525 czernieckik@sullcrom.com

Sydney
Waldo D. Jones Jr.  +61-2-8227-6702 jonesw@sullcrom.com

Beijing
Gwen Wong  +86-10-5923-5967 wonggw@sullcrom.com

Tokyo
Keiji Hatano  +81-3-3213-6171 hatanok@sullcrom.com

Hong Kong
Garth W. Bray  +852-2826-8691 brayg@sullcrom.com
Michael G. DeSombre  +852-2826-8696 desombrems@sullcrom.com
Chun Wei  +852-2826-8666 weic@sullcrom.com
5% increase in total number of publicly announced campaigns against U.S. issuers

Elliott, Starboard and Spruce Point lead the way with the most publicly announced campaigns against U.S. issuers

Infrequent activists bring 68% of all publicly announced campaigns, up from 56%

56% increase in board seats obtained per announced 2018 campaign, as activists on average obtained 0.8 board seats per campaign

Issuers with market capitalizations between $1 – $10 billion targeted in 40% of announced 2018 campaigns despite comprising only 21% of Russell 3000 companies

37% of activist campaigns focus on M&A objectives, up from 26%

Proxy contests focusing on board-related governance matters decrease significantly from 51% to 14%

Proportion of publicly filed settlement agreements expressly permitting information sharing with the activist fund drops from 18% to 7%
Introduction

On the surface, the 2018 activism data is largely consistent with 2017, but with an uptick in overall activity. The amount of capital invested in new activist positions in 2018 was up approximately $2.5 billion from 2017, and activists won more board seats in 2018 than in 2017, mostly through settlements. Although several well-known activists (including Third Point, Pershing Square and Greenlight Capital) announced disappointing investment results in 2018, and the industry experienced negative net asset flows overall, activist funds continue to attract substantial new capital.
While Elliott was the most active fund globally in 2018, accounting for 9% of all campaigns, many other established activists were busy: nine of the top ten activist funds (calculated by aggregate market value of their activist positions at year-end 2018) each invested more than $1 billion in new campaigns in 2018. ² 52% of all board seats won globally since 2013 have been won by a group of 11 activists (in order of board seats won): Starboard, Elliott, Icahn, JANA, Engaged Capital, Sarissa Capital, ValueAct, Corvex, FrontFour, Glenview and Legion Partners.³ Many of these “name brand” activists have since spun-off new funds, or their key players have moved on to other funds, leading to a dispersion of skills and techniques across a wide playing field and resulting in 2018 producing a record number of first-time activists initiating campaigns.

Some activists are also doubling down on their strategies. For example, JANA recently announced it is closing its long/short equity funds to focus on activism and impact investing.⁴ Additionally, if there were a market downturn in 2019, the lower entry point for activists would make investments more affordable in companies perceived to be undervalued. In the last four years, when the S&P 500 has decreased year-over-year and the median VIX has increased year-over-year (2014 to 2015 and 2017 to 2018), we have observed increases in the total number of publicly announced activist campaigns. Conversely, during the same four-year period, we have observed decreases in public activist activity in those years in which the S&P 500 has increased year-over-year and the median VIX has decreased year-over-year.⁵

The consistency of 2018’s data with 2017’s data across multiple metrics suggests that activism practices have begun to stabilize. However, the data alone does not tell the full story, as there have been a few notable trends emerging in the past year. These include: (1) the rise of “purpose” investing; (2) rising prospects for increased civility in activist contests; (3) the changing regulatory landscape; (4) developing technologies that are altering the ways activists and issuers alike can reach shareholders; (5) increased focus on M&A objectives in activism campaigns, including post-deal announcement; and (6) a heightened focus on CEO succession. In addition, more companies are prepared for activists, and activists’ strategies are less likely to seem novel or catch large issuers by surprise. Further, more advisors have entered the activism space, resulting in a proliferation of information about how to engage with activists and other shareholders.

1 Based on aggregate value of new activist positions calculated as of campaign announcement date and not inclusive of derivative positions. See Lazard’s Shareholder Advisory Group, 2018 Review of Shareholder Activism.
2 See Lazard’s Shareholder Advisory Group, 2018 Review of Shareholder Activism.
3 See id.
4 See Wall Street Journal, Jana Is Closing Two Hedge Funds That Lost Money in 2018 (Jan. 15, 2019).
5 Based on information from SharkRepellent.net for U.S. companies with market cap over $100 million. See “Notes on the Scope and Sources of Data Used in This Publication” on page 4.
NOTES ON THE SCOPE AND SOURCES OF DATA USED IN THIS PUBLICATION

The information in this publication on proxy contests and other activist campaigns is based on the database maintained by FactSet Research Systems, Inc. on SharkRepellent.net, using a dataset run on January 15, 2019, supplemented by our review of public information and other third-party sources. To provide an analysis relevant to our U.S. public company clients, we have not included campaigns at companies with a market cap of under $100 million and have not included campaigns at non-U.S. companies. We have followed the SharkRepellent categorization of campaigns as “proxy fights” or “other stockholder campaigns,” but have not included those categorized merely as exempt solicitations or Schedule 13D filings with no public activism. We have not included the mere submission of Rule 14a-8 proposals as “campaigns,” although the section “Types and Objectives of Activist Campaigns” discusses the use of shareholder proposals that were brought in conjunction with the activist campaigns covered in this publication. We have also excluded from the “other stockholder campaigns” category strategic acquisition attempts that involve unsolicited offers by one business entity to acquire another, though we have included takeover attempts involving unsolicited offers by activist hedge funds. In addition, where one activist launched campaigns against several affiliates we counted this as one campaign for purposes of comparison and analysis. Further, we have categorized activist campaigns based on the calendar year in which a campaign was launched, even if the campaign is completed (e.g., an activist gains a board seat) during the following calendar year.

Data in this publication regarding hedge fund assets under management (AUM), performance and formation is based on the year-end 2018 Hedge Fund Industry Report issued by Hedge Fund Research (HFR) on January 18, 2019, unless otherwise indicated. Other data sources, including Proxy Pulse (a Broadridge and PricewaterhouseCoopers initiative), are identified as they arise.

Our analysis throughout this publication is heavily dependent upon this data, statistics, our anecdotal experience and various assumptions. If our assumptions prove to be incorrect or if the data is incomplete or contains errors, our analysis and conclusions could change. Moreover, every activism situation is unique and none of the statistics and analysis presented in this publication should be construed as legal advice with respect to any particular issuer, activist or set of facts and circumstances.
# Table of Contents

1. **TRENDS IN SHAREHOLDER ACTIVISM** ............................................... 8
   A. INTEGRATING “PURPOSE” AND ACTIVISM ........................................ 8
   B. RISING PROSPECTS FOR MORE CIVILITY IN ACTIVISM SITUATIONS ........ 10
   C. REGULATORY CONSTRAINTS ON ACTIVISTS ...................................... 11
   D. CUTTING EDGE SHAREHOLDER COMMUNICATIONS IN ACTIVISM CAMPAIGNS .13
   E. M&A AS A CONSISTENT OUTPUT OF ACTIVISM .................................... 14
   F. SUCCESSION VACUUMS AS A LEADING INDICATOR OF ACTIVISM ............... 14

2. **ACTIVIST INVESTORS** ........................................................................ 16
   A. TOTAL ACTIVIST CAMPAIGNS .............................................................. 16
   B. ASSETS UNDER MANAGEMENT BY ACTIVIST HEDGE FUNDS .................. 16
   C. ACTIVIST HEDGE FUND WITHDRAWALS AND REDEMPTIONS ................ 17
   D. ACTIVIST HEDGE FUND PERFORMANCE ............................................. 17
   E. INCREASE IN ACTIVIST CAMPAIGNS BROUGHT BY INFREQUENT ACTIVISTS . 18
   F. FREQUENT ACTIVIST INVESTORS ...................................................... 19
   G. PROMINENT ACTIVIST INVESTORS .................................................... 20
   H. MOST SUCCESSFUL ACTIVISTS BY BOARD SEATS OBTAINED .................. 20

3. **TARGET COMPANIES** ....................................................................... 22
   A. TARGET COMPANIES BY MARKET CAPITALIZATION .............................. 22
   B. INDUSTRIES OF TARGET COMPANIES ............................................. 23

4. **INSTITUTIONAL INVESTORS** ............................................................... 24
   A. CONCENTRATION AMONG LARGEST INSTITUTIONAL INVESTORS .......... 24
   B. SHIFT FROM RETAIL TO INSTITUTIONAL OWNERSHIP ...................... 25
Broadly speaking, shareholder activism is the practice of purchasing an issuer’s shares with the primary intention of influencing the corporate strategy or governance of the issuer. Our annual shareholder activism study does a deep dive into the data underlying U.S. activism activity to elucidate trends.

A. INTEGRATING “PURPOSE” AND ACTIVISM

Index funds provide virtually permanent capital for corporations. For many years, issuers argued that activists engaged in “short-term” thinking, as reflected in proposed financial engineering strategies designed to shake loose a quick special dividend or share buyback. There was a time when the “long termism” of index funds was seen as a potential boon to companies defending against “short term” activists, and it is true that index funds, on the whole, have been less likely to support activists than other kinds of institutional investors. However, index funds have not as consistently voted against activists as once hoped.

In our most recent annual proxy season memo (available here), we noted the rise of environmental, social and political (ESP) related shareholder proposals and voting policies of proxy advisors and institutional investors. Investor focus on these issues persisted well after the culmination of the 2018 proxy season, with the governance “industry” adapting to this focus by promulgating “sustainability scorecards” and promoting “disclosure enhancements” to address human capital management, sustainability and other ESP-oriented topics. Recently, several of the largest institutional investors reaffirmed this trend with clear statements that they continue to be intensely focused on issuers’ “purpose,” how corporations treat their employees, communities and other stakeholders (not just shareholders), and similar concepts. In his annual letter to CEOs, for example, Larry Fink (CEO of BlackRock) described “purpose” as “a company’s fundamental reason for being – what it does every day to create value for its stakeholders.”

1 See Alon Brav et al., Picking Friends Before Picking (Proxy) Fights: How Mutual Fund Voting Shapes Proxy Contests (Mar. 1, 2018) (finding that passive funds are more friendly towards management and less likely to vote in favor of dissidents/activists than other types of funds). The biggest institutional investor supporters of activists in proxy fights from 2013-2018 were T. Rowe Price, GS Asset Management and JP Morgan Investment Management.

2 See Moelis & Company, Activist Shareholder Advisory Discussion Materials (Jan. 2019) (finding that, since the beginning of 2011, each of the “Big 4” index funds has supported the dissident card in about one of every four proxy contests voted, with BlackRock leading the pack, voting for the dissident card 29% of the time).

This additional focus on “purpose” and stakeholders appears to be part of a larger sociopolitical trend that is reflected in a swell of populism, frustration with income inequality and faith lost in the social and environmental by-products of Adam Smith’s invisible hand. In the political forum, this trend has manifested in the form of legislative action (Senator Warren’s effort to federalize corporations, California’s quotas for female directors and Senator Sanders’ and Senator Schumer’s push to limit stock buybacks, for example). However, both State Street and BlackRock have stressed that their advocacy for a broader perspective on corporate value not be construed as their having a political or social agenda. Indeed, their approach contrasts sharply with some frequent shareholder proponents like the NCRPP, which has an overtly political/social agenda. Instead, both BlackRock and State Street have linked their purpose-driven agenda to a value proposition intended to satisfy their fiduciary duty to their own investors, not to mention ERISA’s fiduciary requirements.

Because winning the largest index funds over is crucial in any activism situation, given the explosive growth of these funds over the past few years (as discussed further in the section “Institutional Investors” below), one might expect to see activists trying to attract support from institutions with arguments about “stakeholders” and “purpose.” However, this behavior was not an observable trend in 2018: the year’s heightened focus on ESP and “purpose” often seemed like it was just background noise in activism campaigns. Specifically, notwithstanding institutional investors’ calls for more gender diversity on boards, only 18% of activist appointees in 2018 were female, as compared to 40% of new S&P 500 directors in 2018. We are not aware of an index fund failing to support an activist merely because the activist publicly presented an all-male slate. An ISS study recently confirmed that, in the aggregate, activist appointees do not promote gender or racial/ethnic diversity, and activists’ slates in contested elections are dominated by investment professionals and a mix of former and sitting executives. The largest index funds appear to have given the activists a pass on the lack of diversity in their slates.

However, it remains to be seen whether the focus on ESP and “purpose” will become more meaningful for activist funds in the coming years. Notably, two former investing partners at Blue Harbour Group recently launched Impactive Capital, an activist investment firm seeded by CalSTRS that will engage with companies over ways

---

4 See Lazard’s Shareholder Advisory Group, 2018 Review of Shareholder Activism.
6 This may be exacerbated by the fact that very few women serve in senior roles at activist funds. As of February 2019, a mere 11.2% of senior positions at hedge fund managers were occupied by female employees. See Preqin, Women in Hedge Funds (Feb. 2019).
to improve capital allocation and ESP practices.⁸ We may start to see more overt efforts by activists to challenge incumbent management teams and boards for neglecting to focus on long-term attributes of profitability, and seeking to position themselves as partners in institutional investors’ efforts to bring more focus and accountability to identifying directors’ skills and capabilities. We would not be surprised to see an activist attack a coal company or gun or opioid manufacturer for failing to have more socially responsible practices, or target a natural resources company for having ineffective risk management in relation to its environmental practices. We may also see activists focus on executive compensation not only as an avenue for righting perceived poor governance and mismanagement at target companies, but also for drawing focus to issues like human capital management and corporate culture—though this may be a more difficult avenue for activists than other ESP initiatives given the overwhelming support for say-on-pay votes at public companies.⁹

B. RISING PROSPECTS FOR MORE CIVILITY IN ACTIVISM SITUATIONS

Aggressive activist attacks are legendary, from stories of activists going through a CEO’s literal and figurative garbage to examples of directors being tailed by activists on social media and at cocktail parties.¹⁰ These extreme investigative tactics are presumed to be a stepping stone to a damning out-of-the-blue public letter that will disrupt the target’s ownership profile by attracting arbitrageurs who are more likely to be seeking a short-term profit than long-term operational success. They also can create so much embarrassment for the CEO and directors that they concede and/or resign.

However, a recent article reviewed a more civil style of activist tactics as “soft” activism, emphasizing the importance of behind-the-scenes engagement.¹¹ Some activists are reportedly toning down their rhetoric and taking measures to soften their image (perhaps in a bid to appeal to the governance groups at the index funds).¹² If civility of discourse in activism situations is in fact a growing trend, it should enhance management teams’ ability to stay focused on their “day jobs” of running businesses without the distractions brought on by responding to a steady stream of attacks.

---

⁹ See Sullivan & Cromwell LLP, 2018 Proxy Season Review (July 2018) (finding that support levels in say-on-pay votes exceeded 90% on average at public companies during the 2018 proxy season).
and potential resulting vulnerability that can be a by-product of escalating PR battles in an activism contest.

Nonetheless, directors need to be resolute in their position and advised about the worst-case scenario. In this regard, directors should be updated periodically about activism and review their structural defenses to ensure they conform to best practices and provide the company with adequate time to respond to an activist attack. Companies also need to continue to be vigilant for short-sellers and “debt squeeze” tactics that can adversely impact public shareholders.\(^{13}\) The success of Third Point’s campaign at Campbell (despite Campbell being approximately 41% owned by its founding family) is a good reminder that even with market-standard defenses and vigilance, no company should assume it is immune from activism.

C. REGULATORY CONSTRAINTS ON ACTIVISTS

In the past few years, and especially in 2018, several governmental entities showed an appetite for enforcing their regulations against activists. Among other things, regulators have begun to focus on the following issues that may be relevant to activism contests:

1. **Director interlocks.** Where activists have designated directors on the boards of multiple companies in the same industry, they may run afoul of Section 8 of the Clayton Act (or in the case of banks, the Depository Institution Management Interlocks Act), which restricts interlocking directors on the boards of competitors. Notably, in January, ValueAct agreed to an information sharing arrangement with Citi rather than seeking a board seat, because the activist already had a board seat at one of Citi’s competitors, Alliance Data Systems, creating a perceived conflict.\(^{14}\) This may be an issue even where the individual directors are different people if the activist is deemed to have “deputized” the individuals. In that case, those directors may be seen as a conduit for sharing competitively sensitive information among competitors. Note, however, that regulator-initiated action does not appear to have dictated any activist behavior in this area, as activists have generally tended to avoid this practice.

2. **Industry specific regulations.** Certain industries, especially banking, insurance and public utilities, may be subject to change

---

\(^{13}\) Short sale strategies continued to be used by activists in 2018, including by Spruce Point in its approach of 2U, Inc. and Kynikos in its approach of Dunkin’ Brands. Activists also continued their historic use of “debt default activism”—a term used to describe the strategy whereby an activist purchases distressed debt and seeks to enforce a default. In 2018, Aurelius Capital Management used this tactic in its approach of Windstream Holdings, which ended in Windstream filing a voluntary petition under Chapter 11 to seek bankruptcy protection after it lost a lengthy court battle with the activist. Some have accused Neiman Marcus bondholders of using a similar strategy in recently agreeing to extend the term of the company’s outstanding bonds. See Bloomberg, *Neiman Marcus Struck 'Devils Bargain' With CDS Traders, Fund Says* (Mar. 4, 2019).

\(^{14}\) See Bloomberg, *Citigroup Agrees to Give Activist ValueAct Details on Strategy* (Jan. 11, 2019).
of control and other restrictions that could be implicated in activism contests. For example, Washington banking regulators stepped in when a shareholder activist, Roaring Blue Lion, initiated a proxy contest for HomeStreet, a Washington bank. The regulator issued an interpretive letter determining that there was a “substantial risk” that the company could not count votes on the activist’s proxy card, including for quorum purposes, because the proxies would essentially amount to a conveyance of controlling influence over a bank that had not been approved by the regulator. Activists preparing to approach a banking institution should also carefully consider the Depositary Institution Management Interlocks Act, which generally prohibits management officials of a depositary organization from serving in a management role at another depositary organization where that service could have an anti-competitive effect.

3. **13D and HSR enforcement actions.** The SEC has reported enforcement actions relating to violations of Rule 13(d)’s beneficial ownership reporting requirements (both as to the timing of initial filings as well as to the obligation promptly to update existing filings to reflect a change in investment or voting intent). Issuers have also, from time to time, requested that the SEC consider whether activists should be deemed to have formed a 13(d) group given the conscious parallelism of their behavior towards certain issuers that are the subject of side-by-side campaigns. The DOJ has also cracked down on activists failing to file HSR notifications in relation to acquisitions of common stock in excess of the reporting threshold, purportedly in reliance on the passive intent exception.

4. **Common ownership.** Although not directed at activists, the Commissioners of both the FTC and the SEC have noted that the competitive effects of common ownership by institutional investors, especially index funds (the top-three of whom now collectively hold approximately 19% of the S&P 500) deserve to be studied. This issue has become an area of focus due to assertions that having such large shareholders exerting common influence could dampen competition among public companies. A recent academic study, however, argued that this concern is misplaced on the basis that the funds are not actually exerting that kind of influence in practice.

---


Regulatory defenses are not a panacea for issuers seeking to fend off an activist attack, but recent enforcement actions have certainly put activists on notice that they ought to evaluate their regulatory profile before engaging in a campaign.

### D. CUTTING EDGE SHAREHOLDER COMMUNICATIONS IN ACTIVISM CAMPAIGNS

Special-purpose websites and alternative media were once the purview of mega-cap M&A transactions, but activists are increasingly using these techniques in their campaigns as well. 2018 saw a surge in the use of electronic media in proxy contests, such as activists posting YouTube videos and sending out flash drives filled with “pro-change” information to investors. For example, in the Third Point-Campbell Soup contest, Third Point posted a four-minute video to YouTube imploring shareholders to elect the activist’s board slate and #RefreshTheRecipe.19 The use of these techniques is more common in relation to large-cap issuers, where the campaigns are higher profile and the activist often has to make a more sizeable investment to make its mark. This is especially true for those large companies that have a relatively high proportion of retail investors, whose historically low voting rates can be boosted by enhanced communication efforts. At this stage, these techniques are not widely used against small cap companies, even though they are the most frequent targets of activists. The dearth of flashy e-campaigns against small caps is probably attributable to the relative costs and benefits of “high production value” material in those campaigns. However, as activists develop new templates, the variable cost of employing these techniques in smaller campaigns will inevitably shrink and they will become more prevalent.

The media strategies of the companies the activists target will need to evolve to keep pace with the activists—not just in the midst of a proxy contest but also as an important tool for good communication of key messages to investors in the off-season.

---

19 See https://www.youtube.com/watch?v=DLptfL5jPDg.
IPO, issuers increasingly view quality investor communications (not just media relations) as a key element of retaining investor support.

**E. M&A AS A CONSISTENT OUTPUT OF ACTIVISM**

It has been clear for many years that activism catalyzes both friendly and unsolicited M&A because activists often drive efforts to put a company up for sale or engage in divestitures. Whether or not a company actually initiates a strategic review process (code for “sale or divestiture”) in response to an activist campaign, the attention generated by the activist may attract interest from unsolicited acquirors.

According to Lazard, 33% of 2018 activism campaigns were M&A-related. Of these: 41% pushed for the sale of the company; 28% pushed for a break-up or divestiture; and 30% sought to intervene in an announced deal, seeking a price bump or a termination of the deal. Examples of activists interfering in announced transactions in particular have surged, and include Carl Icahn’s opposition to the Cigna/Express Scripts and Dell/VMware transactions, and Krupa Global Investments’ opposition to Kraft Heinz participating in the auction for Campbell’s international business before there was even an announced deal on the table.

In a few high-profile incidents, the activists themselves have become the hostile acquirors, their campaigns turning into takeover bids by their own private equity affiliates. Notably, Elliott now has an active private equity arm that has engaged in some high-profile bidding, suggesting a convergence of activist hedge funds and traditional private equity. In January, Elliott asked investors for $2 billion to pursue take-private transactions. Activists must carefully consider securities laws in the M&A context, particularly where the activist obtains material non-public information in the course of discussions with the issuer or where the activist teams up with a strategic acquiror (e.g., Allergan-Valeant).

**F. SUCCESSION VACUUMS AS A LEADING INDICATOR OF ACTIVISM**

A common theme in activist campaigns is an effort to oust a sitting CEO, such as Starboard Value’s and others’ campaign to push out the CEO of MGM Resorts. Less overt is activist involvement in companies that lack a permanent CEO, or that have an impending CEO retirement. Those cases may provide activists with the ability to have outsized influence in the selection of the next management team. It is unclear if activist involvement at this stage in a company’s life cycle actually makes it more difficult for a board to attract necessary talent (i.e., are there potential CEO candidates who would turn down...

---

the role because an activist is present). What is clear is that any company expecting to undergo a CEO transition in the next couple of years would be wise to do some careful planning to ensure that the board’s preferred candidate is identified well in advance of any public announcements, or significant speculation, regarding a transition, if possible, and investors have a clear picture of the board’s focus and priorities with regard to succession planning. A company’s public announcement of the CEO transition must be thoughtfully structured to instill investor confidence in the board’s decision.
A. TOTAL ACTIVIST CAMPAIGNS

2018 saw a 5.5% increase in the number of activist campaigns, with 268 campaigns announced. The total number of campaigns has been remarkably consistent over the past five years with an average of approximately 272 campaigns announced per year. However, the total number of public campaigns in a given year does not paint a full picture; based on anecdotal information, a significant number of activist situations also are being resolved without publicity.

Proxy contests made up a slightly smaller percentage of announced activist campaigns in the past three years than had been observed in prior years. During these three years, less than 20% of activist campaigns developed into proxy contests. In comparison, full-scale proxy contests developed, on average, in slightly less than one-quarter of all activist campaigns announced in 2014 and 2015. Importantly, this statistic does not take into account campaigns that were settled prior to developing into a proxy contest but still resulted in board seats for the activists.

B. ASSETS UNDER MANAGEMENT BY ACTIVIST HEDGE FUNDS

In 2018, activist hedge fund AUM showed modest decreases, shrinking at a meaningfully higher rate than hedge funds overall. The second half of 2018 was the first period since the first half of 2016 that activist hedge fund AUM declined, reversing a two-year period of continued growth. Note that the changes in AUM during the second half of 2018 may be largely attributable to overall market performance
and the differences in the portfolio composition of activist funds compared to non-activist funds. The decrease in non-activist hedge fund AUM tracked the Dow Jones Industrial Average (-3.84% and -3.89%, respectively) while the decrease in activist hedge fund AUM tracked the S&P 500 (-7.76% and -7.78%, respectively).

C. ACTIVIST HEDGE FUND WITHDRAWALS AND REDEMPTIONS

Activist hedge funds experienced negative net asset flows in each of the last three quarters of 2018, resulting in a total negative net asset flow of approximately $2.18 billion in 2018. Despite a brief period of positive net asset flow from mid-2017 through the first quarter of 2018, the negative net asset flow in 2018 represented a shift back to the previous trend of negative net asset flows from the fourth quarter of 2015 until mid-2017. Net outflows at activist hedge funds represented approximately 2% of average AUM during this period, whereas outflows at all hedge funds represented just over 1% of average AUM.

The disproportionate amounts of outflows from activist hedge funds over the last three years suggest, at a minimum, that these funds may face significant fundraising and fund-retention challenges when seeking to identify and capitalize on activism opportunities in the near-term.

D. ACTIVIST HEDGE FUND PERFORMANCE

In 2018, the hedge fund industry as a whole earned low returns—an average of negative 0.54% per quarter—and activists underperformed the hedge fund industry by posting average returns of negative 1.12% per quarter. In general, activist hedge funds have been more volatile than hedge funds overall, and this volatility has continued through recent years. Hedge funds significantly outperformed the S&P 500.
and the Dow Jones Industrial Average in 2018, which had returns of negative 6.2% and negative 5.6%, respectively.\footnote{MarketWatch, \textit{Here’s How Ugly 2018 Was For Stocks and Other Assets} (Jan. 1, 2019).}

**E. INCREASE IN ACTIVIST CAMPAIGNS BROUGHT BY INFREQUENT ACTIVISTS**

Over the past several years, the percentage of campaigns launched by “infrequent” activist investors has increased and 2018 marked a continuation of this trend. For purposes of this publication, we have defined infrequent activists as firms that have brought five or fewer campaigns since the beginning of 2014. Infrequent activists brought 57% of all proxy contests and 68% of all publicly announced campaigns in 2018, marking an increase from 2017 when infrequent activists brought 54% of all proxy contests, but only 56% of all announced campaigns. The level of infrequent activist activity in 2018 was more consistent with 2016 levels.
F. FREQUENT ACTIVIST INVESTORS

The most frequent activists in terms of announced campaigns against U.S. issuers in 2018 were Spruce Point, Elliott Management and Starboard. In addition to the public campaigns discussed below, activists engage in “behind the scenes” campaigns that often prove successful. Elliott is the only activist to appear in the top-three of announced campaigns in each of the past four years. During this time period, Elliott has engaged in 34 announced campaigns against U.S. issuers. This is the first time Spruce Point, a long/short hedge fund founded in 2009 that focuses on short selling activism strategies, has appeared in the top-three over the past five years, but it was active last year as well, announcing seven campaigns in 2017. GAMCO, which had been in the top-three from 2014 through 2017, announced one campaign against a U.S. issuer in 2018:

Announced U.S. Campaigns by Most Frequent Activists

<table>
<thead>
<tr>
<th>Year</th>
<th>Activist Name</th>
<th>Campaigns</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>Spruce Point Capital Management LLC</td>
<td>9</td>
</tr>
<tr>
<td></td>
<td>Elliott Management Corporation</td>
<td>8</td>
</tr>
<tr>
<td></td>
<td>Starboard Value LP</td>
<td>8</td>
</tr>
<tr>
<td>2017</td>
<td>Elliott Management Corporation</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>GAMCO Asset Management, Inc.</td>
<td>9</td>
</tr>
<tr>
<td></td>
<td>City of London Investment Management Co. Ltd.</td>
<td>9</td>
</tr>
<tr>
<td>2016</td>
<td>Elliott Management Corporation</td>
<td>8</td>
</tr>
<tr>
<td></td>
<td>Bulldog Investors, LLC</td>
<td>7</td>
</tr>
<tr>
<td></td>
<td>GAMCO Asset Management, Inc.</td>
<td>4</td>
</tr>
<tr>
<td>2015</td>
<td>GAMCO Asset Management, Inc.</td>
<td>11</td>
</tr>
<tr>
<td></td>
<td>Bulldog Investors, LLC</td>
<td>9</td>
</tr>
<tr>
<td></td>
<td>Elliott Management Corporation</td>
<td>8</td>
</tr>
<tr>
<td>2014</td>
<td>Starboard Value LP</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>GAMCO Asset Management, Inc.</td>
<td>9</td>
</tr>
<tr>
<td></td>
<td>Lone Star Value Management, LLC</td>
<td>8</td>
</tr>
</tbody>
</table>
G. PROMINENT ACTIVIST INVESTORS

As discussed further in the section “Target Companies by Market Capitalization” below, a large percentage of Fortune 100 companies have been the targets of activist campaigns. But, given the capital required to acquire a significant stake in large-cap companies, only a small number of prominent activist investors have targeted Fortune 100 companies, and only five investors have announced more than two activist campaigns against a Fortune 100 target company since 2014.

<table>
<thead>
<tr>
<th>Activist</th>
<th>Campaigns</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trian Fund Management, L.P.</td>
<td>4</td>
</tr>
<tr>
<td>Third Point LLC</td>
<td>4</td>
</tr>
<tr>
<td>Icahn Associates Corp.</td>
<td>4</td>
</tr>
<tr>
<td>Value Act Capital Management LP</td>
<td>3</td>
</tr>
<tr>
<td>Greenlight Capital, Inc.</td>
<td>3</td>
</tr>
<tr>
<td>Elliott Management Corporation</td>
<td>2</td>
</tr>
<tr>
<td>Glenview Capital Management LLC</td>
<td>2</td>
</tr>
<tr>
<td>JANA Partners LLC</td>
<td>2</td>
</tr>
<tr>
<td>California State Teachers’ Retirement System</td>
<td>2</td>
</tr>
<tr>
<td>Arjuna Capital LLC</td>
<td>2</td>
</tr>
</tbody>
</table>

H. MOST SUCCESSFUL ACTIVISTS BY BOARD SEATS OBTAINED

Activists have experienced higher success rates in obtaining board seats in recent years, although the volume of campaigns has declined markedly since 2015. In 2018, activists averaged 0.8 board seats per campaign, doubling the 2016 average. As summarized in the table below, activists on average have received more than one board seat for every two campaigns announced in a particular year.23

<table>
<thead>
<tr>
<th></th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Board Seats Obtained</td>
<td>169</td>
<td>173</td>
<td>96</td>
<td>114</td>
<td>116</td>
</tr>
<tr>
<td>Number of Total Completed Campaigns</td>
<td>272</td>
<td>300</td>
<td>243</td>
<td>221</td>
<td>143</td>
</tr>
<tr>
<td>Average Board Seats Per Campaign</td>
<td>0.62</td>
<td>0.57</td>
<td>0.40</td>
<td>0.52</td>
<td>0.81</td>
</tr>
</tbody>
</table>

23 For purposes of this section, board seats are recorded as obtained during the year in which the activist campaign was initiated.
The activists that have been the most successful at obtaining board seats are generally those who are the most prolific in terms of number of campaigns. Icahn Associates is a notable exception, in that it has not been in the top-three most frequent activists in any year during the past five years. However, in the campaigns it has announced, Icahn has been remarkably successful, obtaining, on average, 1.48 board seats in each announced campaign over the last five years. Many board seats are also obtained through “quiet” campaigns where an activist engages with the issuer “behind the scenes.” As noted in “Notes on the Scope and Sources of Data Used in This Publication,” this data is limited to U.S. companies, and so does not reflect the success of activist funds, like Elliott, in Europe over the past five years.

<table>
<thead>
<tr>
<th>Number of Board Seats Obtained by Most Successful Activists at U.S. Issuers</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Starboard Value LP</td>
<td>24</td>
<td>13</td>
<td>5</td>
<td>7</td>
<td>12</td>
</tr>
<tr>
<td>Icahn Associates Corporation</td>
<td>5</td>
<td>9</td>
<td>3</td>
<td>0</td>
<td>14</td>
</tr>
<tr>
<td>Elliott Management Corporation</td>
<td>7</td>
<td>6</td>
<td>9</td>
<td>6</td>
<td>5</td>
</tr>
</tbody>
</table>
A. TARGET COMPANIES BY MARKET CAPITALIZATION

Following a sharp increase in 2017 in the percentage of activist campaigns at the largest companies, 2018 saw a reversal of course with a decrease in the percentage of campaigns at the largest companies. This decrease brings the percentage of campaigns at the largest companies roughly in line with 2015 and 2016. In general, the frequency of campaigns in each band of market capitalization has remained relatively steady since 2014. The following table sets forth by market capitalization the percentage of companies targeted by activist campaigns announced since the beginning of 2014, with the first row indicating the allocation of companies in the Russell 3000 Index (the “Russell 3000”) in each range.

Target Company Market Capitalization

<table>
<thead>
<tr>
<th></th>
<th>$100m–$500m</th>
<th>$500m–$1b</th>
<th>$1b–$10b</th>
<th>$10b–$50b</th>
<th>&gt;$50b</th>
</tr>
</thead>
<tbody>
<tr>
<td>Percentage of total companies</td>
<td>21%</td>
<td>14%</td>
<td>40%</td>
<td>12%</td>
<td>3%</td>
</tr>
<tr>
<td>2018 campaigns</td>
<td>40%</td>
<td>13%</td>
<td>34%</td>
<td>8%</td>
<td>3%</td>
</tr>
<tr>
<td>2017 campaigns</td>
<td>41%</td>
<td>16%</td>
<td>29%</td>
<td>7%</td>
<td>6%</td>
</tr>
<tr>
<td>2016 campaigns</td>
<td>44%</td>
<td>19%</td>
<td>29%</td>
<td>6%</td>
<td>2%</td>
</tr>
<tr>
<td>2015 campaigns</td>
<td>45%</td>
<td>15%</td>
<td>29%</td>
<td>8%</td>
<td>3%</td>
</tr>
<tr>
<td>2014 campaigns</td>
<td>42%</td>
<td>14%</td>
<td>33%</td>
<td>6%</td>
<td>5%</td>
</tr>
<tr>
<td>Five-year average</td>
<td>42%</td>
<td>15%</td>
<td>31%</td>
<td>7%</td>
<td>4%</td>
</tr>
</tbody>
</table>

Smaller companies tend to be targeted more frequently, with companies whose market cap is between $100 million and $500 million representing an average of 40% of campaigns in 2018, while representing only 21% of Russell 3000 companies. In contrast, companies with market caps between $1 billion and $10 billion are less likely to be targeted than their representation as a percentage of Russell 3000 companies suggests, as these companies represent an average of 31% of campaigns, while making up 40% of Russell 3000 companies.

On average, approximately 11% of the campaigns in each year targeted companies with market caps of greater than $10 billion, with companies with market caps of greater than $50 billion making up around 4% of total campaigns. Although companies with market caps greater than $50 billion made up 6% of total campaigns in 2017 (while representing only 3% of Russell 3000 companies), the same category...
made up only 3% of total campaigns in 2018. Despite this decrease, the past five years have made it clear that the largest companies are in no way immune from activist campaigns. For the companies that are currently in the Fortune 100, 25% have been targeted by a public activism campaign since 2013 and many others have dealt privately with activism situations.

B. INDUSTRIES OF TARGET COMPANIES

Activists have targeted a wide variety of industries since 2014. The most targeted industries, which have generally remained consistent in each year, include investment vehicles (including investment trusts and mutual funds), pharmaceutical companies, software companies and other commercial service providers.

**Most Targeted Industries 2014 to 2018**

<table>
<thead>
<tr>
<th>Industry</th>
<th>Total Campaigns</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real Estate Investment Trusts</td>
<td>79</td>
</tr>
<tr>
<td>Investment Trusts / Mutual Funds</td>
<td>71</td>
</tr>
<tr>
<td>Packaged Software</td>
<td>70</td>
</tr>
<tr>
<td>Integrated Oil</td>
<td>52</td>
</tr>
<tr>
<td>Miscellaneous Commercial Services</td>
<td>43</td>
</tr>
<tr>
<td>Pharmaceuticals: Major</td>
<td>39</td>
</tr>
</tbody>
</table>

One particular industry that has been targeted in 2018 more than in years past was integrated oil, which includes businesses engaging in the production, exploration, refinement and distribution of oil and gas. There were 22 campaigns announced against integrated oil companies in 2018 compared to an average of just over seven per year from 2014 through 2017.

---

24 Industry classifications based on data from SharkRepellent.net. See “Notes on the Scope and Sources of Data Used in This Publication” on page 4.
The influence of large index funds and other institutional investors is central to outcomes of shareholder activism contests. Despite the growth of activist investing in recent years, activists in the aggregate hold a very small percentage of public company stock. Even in companies where they launch campaigns, activists usually do not hold enough stock for those holdings to play a determinative role in vote outcomes. For campaigns launched in 2018, the median percentage ownership of the dissident group was approximately 7% and was less than 2% at companies with a market cap of over $20 billion. In many cases, an activist will have additional exposure to the target through various derivative positions, but those positions often do not give the activist the right to vote the underlying shares.25

In any event, in order to succeed in proxy contests or other campaigns, activists depend on the support of large institutional investors. These large investors, particularly index fund managers, are well aware of their critical role. Accordingly, before turning to a detailed discussion of the types and objectives of activist campaigns, this section highlights trends among the large institutional investors.

A. CONCENTRATION AMONG LARGEST INSTITUTIONAL INVESTORS

Concentration of equity ownership, particularly among the largest three index fund providers, continues to be a key component in the activism landscape. As of December 2018, one of BlackRock, Vanguard or State Street was the largest shareholder in 438 of the S&P 500 companies, roughly 88 percent, and collectively the three firms owned 18.7% of all shares in the S&P 500.26 Fidelity is the fourth-largest institutional investor and its ownership also significantly contributes to the equity concentration of the S&P 500.

In prior memoranda, we have discussed the possibility that universal proxy cards, in which management and shareholder nominees are included on a single ballot rather than two separate ballots, could make this concentration of share ownership even more impactful. We observed that if a dissident shareholder could trigger the use of

25 Where an activist investor uses derivative positions to hedge its exposure to an issuer, some have argued that this weakens the activist’s argument that it is aligned with other shareholders. For example, in Elliott’s approach of Telecom Italia, it used a “collar” to protect a portion of its stake, leading Telecom Italia’s largest shareholder, Vivendi, to argue that Elliott’s interests were misaligned with other shareholders. See The Wall Street Journal, How Activists Buy Two Votes With One Share (Mar. 4, 2019).

a universal proxy card by reaching out to a small number of large shareholders, it would be much less costly for activists to run a proxy contest. The topic gained renewed traction this year when, in June 2018, SandRidge Energy used the first-ever universal proxy card in its proxy contest with Carl Icahn. A universal proxy card was also proposed in proxy contests with Cars.com and Mellanox Technologies over the course of the year. Although the renewed interest has not led to regulatory change, the SEC implied that it remains open to the idea by including it on the agenda of items discussed at the Roundtable on the Proxy Process held on November 15, 2018.

B. SHIFT FROM RETAIL TO INSTITUTIONAL OWNERSHIP

There continues to be a significant difference between the levels of retail and institutional ownership of public companies. Over the past three years, retail ownership of all U.S. public companies has hovered around 30%. Meanwhile, as of September 30, 2018, companies in the S&P 500 were approximately 84% owned by institutional investors.

The difference between retail and institutional ownership underscores the relative voting power exercised by institutional investors. In 2018, consistent with past years, only 28% of retail-held shares were voted, compared to 91% of shares held by institutions. The difference in voting participation is the result of several factors.

- First, in many cases, institutional investors are required to vote their shares because of fiduciary duties, while there is no requirement for retail investors to vote their shares.
- Second, the use of notice-and-access for delivery of proxy materials to shareholders has contributed to declining voter participation among retail investors.
- Third, the diminishing voting participation of retail shareholders has been amplified by the elimination of broker discretionary voting on uninstructed “street name” shares.

As institutional investors continue to amass voting power, they also are becoming significantly more self-reliant in making voting determinations. The frequency with which many of the largest

As of December 2018, one of BlackRock, Vanguard or State Street was the largest shareholder in 438 of the S&P 500 companies, roughly 88 percent.

---

30 Based on data from FactSet Research Systems, Inc. as of February 1, 2019, sourced from Form 13-F filings.
31 ProxyPulse, 2018 Proxy Season Review. This relates to overall votes; not merely contested matters.
32 The concerns over reduced retail participation when notice-and-access is used are discussed in SEC Release No. 33-9108 (Feb. 22, 2010).
in institutional investors vote with ISS and Glass Lewis has dropped in the last three years; for example, BlackRock’s voting alignment with ISS has dropped from 61% in 2016 to 31% in 2018.33

The multi-tiered system of beneficial ownership of U.S. equity securities continues to complicate efforts to verify the legitimacy of investor participation in proxy contests. The Trian campaign at P&G, where it took the inspector of elections 66 days to finalize the vote count, is one high-profile example of the shortcomings of this system. In 2018, proxy voting reform continued to be an area of focus in the industry and was a key discussion point at the SEC Investor Advisory Committee meeting, held on September 13, 2018.34 Further, Broadridge has reportedly spent approximately $150 million looking into how to use blockchain technology to innovate proxy voting (and other applications).35 In March 2018, Broadridge teamed up with Santander to pilot a blockchain ballot at Santander’s annual meeting.36

This comes after the July 2017 announcement that Delaware had amended the Delaware General Corporation Law to include several blockchain-related provisions, including the possibility of using blockchain technology to create and administer stock ledgers.37

34 Pensions & Investments, Drumbeat grows louder for proxy voting reforms (Oct. 1, 2018).
35 See Barrons, Blockchain Could Help Fix Proxy Voting Problems (July 6, 2018).
36 See Financial Times, Santander shows potential of blockchain in company votes (May 17, 2018). Approximately one-fifth of Santander’s shareholders utilized the blockchain system, which Santander considered a “true success.” See Barrons, Blockchain Could Help Fix Proxy Voting Problems (July 6, 2018).
Initiating or threatening to initiate a proxy contest for board representation is a common strategy used by activists to achieve their campaign objectives. A proxy contest occurs when an activist nominates one or more directors for election in opposition to a public company’s slate of director nominees. Activists also conduct campaigns through other avenues and tactics, all of which we have included in the general category of “other stockholder campaigns”; this can include publicly disclosing letters to target companies, issuing press releases, proposing precatory or binding shareholder proposals, running “vote no” campaigns against incumbent directors, calling special meetings or taking actions by written consent.

**A. FREQUENCY OF DIFFERENT CAMPAIGN TYPES**

2018 saw a 5.5% increase in the number of activist campaigns, including both proxy contests and other stockholder campaigns, following a slight reduction in 2017. The number of activist campaigns in 2018 was generally in line with five-year averages.

**Number of Campaigns Announced Per Year**

<table>
<thead>
<tr>
<th></th>
<th>Proxy Contests</th>
<th>Other Stockholder Campaigns</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>51</td>
<td>217</td>
<td>268</td>
</tr>
<tr>
<td>2017</td>
<td>47</td>
<td>207</td>
<td>254</td>
</tr>
<tr>
<td>2016</td>
<td>49</td>
<td>218</td>
<td>267</td>
</tr>
<tr>
<td>2015</td>
<td>73</td>
<td>227</td>
<td>300</td>
</tr>
<tr>
<td>2014</td>
<td>62</td>
<td>210</td>
<td>272</td>
</tr>
<tr>
<td>Five-year average</td>
<td>56</td>
<td>216</td>
<td>272</td>
</tr>
</tbody>
</table>

On average, approximately 21% of activist campaigns have taken the form of actual proxy contests in the past five years. The actual percentage of proxy contests compared to total announced campaigns in 2018 was slightly below average at 19%, but this number can be explained in part by the fact that some of the campaigns currently categorized as “Other Stockholder Campaigns” may yet evolve into actual proxy contests in 2019.
B. UNDERLYING OBJECTIVES OF ACTIVIST CAMPAIGNS

Although board representation remains the most common objective in activist campaigns, it is almost always sought in conjunction with other underlying objectives. In past years, the most common underlying objectives of proxy contests related to business strategies, balance-sheet actions (such as returning cash to shareholders through dividends or share repurchases, which are often related to capital allocation strategies) and divestitures or other M&A actions (such as encouraging a sale of the company or opposing a merger). In 2018, proxy contests focused mostly on balance-sheet issues (such as concerns about the capital structure of the company) and M&A actions. The number of proxy contests focusing on board-related governance fell dramatically in 2018 after seeing a jump in 2017, and fell far below the five-year average.

Objectives of Proxy Contests

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Business Strategies</td>
<td>44%</td>
<td>34%</td>
<td>21%</td>
<td>15%</td>
<td>12%</td>
<td>25%</td>
</tr>
<tr>
<td>Balance Sheet</td>
<td>35%</td>
<td>53%</td>
<td>21%</td>
<td>60%</td>
<td>25%</td>
<td>39%</td>
</tr>
<tr>
<td>M&amp;A</td>
<td>27%</td>
<td>40%</td>
<td>21%</td>
<td>13%</td>
<td>27%</td>
<td>26%</td>
</tr>
<tr>
<td>Board-Related Governance</td>
<td>26%</td>
<td>26%</td>
<td>23%</td>
<td>51%</td>
<td>14%</td>
<td>28%</td>
</tr>
<tr>
<td>Compensation</td>
<td>5%</td>
<td>11%</td>
<td>10%</td>
<td>23%</td>
<td>10%</td>
<td>12%</td>
</tr>
<tr>
<td>Other Governance</td>
<td>19%</td>
<td>8%</td>
<td>2%</td>
<td>15%</td>
<td>6%</td>
<td>10%</td>
</tr>
</tbody>
</table>

Underlying Objectives of Other Stockholder Campaigns

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Business Strategies</td>
<td>23%</td>
<td>24%</td>
<td>24%</td>
<td>47%</td>
<td>29%</td>
<td>30%</td>
</tr>
<tr>
<td>Balance Sheet</td>
<td>26%</td>
<td>21%</td>
<td>17%</td>
<td>37%</td>
<td>44%</td>
<td>29%</td>
</tr>
<tr>
<td>M&amp;A</td>
<td>31%</td>
<td>37%</td>
<td>34%</td>
<td>29%</td>
<td>39%</td>
<td>34%</td>
</tr>
<tr>
<td>Board-Related Governance</td>
<td>7%</td>
<td>11%</td>
<td>13%</td>
<td>26%</td>
<td>12%</td>
<td>14%</td>
</tr>
<tr>
<td>Compensation</td>
<td>4%</td>
<td>7%</td>
<td>5%</td>
<td>5%</td>
<td>7%</td>
<td>6%</td>
</tr>
<tr>
<td>Other Governance</td>
<td>0%</td>
<td>2%</td>
<td>1%</td>
<td>3%</td>
<td>5%</td>
<td>2%</td>
</tr>
</tbody>
</table>

38 The percentages in these tables often add up to over 100% because single campaigns often have multiple objectives.
C. TACTICS USED BY ACTIVISTS

The most common tactics in the activist’s playbook (other than nominating a director slate) are publicity campaigns (including publicly disclosing presentations about the company or letters to the company, issuing press releases, establishing websites and using Twitter and social media). In 2018, publicity campaigns largely returned to their pre-2017 levels; activist investors made public disclosures in 40% of 2018 campaigns. Other tactics that are used from time to time, including initiation of litigation and the calling of a special meeting, happen relatively rarely—in less than five percent of campaigns over this period.

D. LITIGATION TACTICS USED BY ACTIVISTS

One less frequent, but important, tool in the activist’s toolbox is the initiation or threat of litigation. Activists have initiated litigation in roughly two to four percent of campaigns each year for the past five years. Some of the more notable campaigns involving litigation by activists in 2018 included: (1) John Schnatter’s attempts to retake control of Papa John’s; (2) Carl Icahn’s opposition to each of AmTrust Financial Services, Inc.’s going private transaction and Dell Technologies, Inc.’s recapitalization to eliminate its VMWare tracking stock; (3) Third Point’s campaign against Campbell’s Soup; (4) Albert Ratner’s unsuccessful attempt to block the acquisition of Forest City Realty Trust (of which he was co-Chairman emeritus and former CEO) by Brookfield Property Partners; and (5) Darwin Deason’s successful efforts to block the Xerox-Fujifilm combination.

Activist-initiated litigation tends to involve Section 220 (books and records) demands, breach of fiduciary duty claims and/or allegations regarding violations of the federal securities laws. Litigation can serve several purposes—in addition to attempting to achieve success on the merits of the claim, activists can use litigation for the purposes of frustration and delay, as an additional platform for airing grievances and as an additional source of pressure on targeted companies and boards. Activists can also leverage interim orders and judgments to bolster their causes (a hollow success on a motion for discovery can be spun in the press as an indication that the underlying claim or agenda has merit, for instance), and use discovery as a tool for ferreting out damaging or embarrassing e-mails and other documents (whether or not ultimately directly related to the matter being litigated). On this last point, the Chancery Court’s ruling in

39 These claims can sometimes raise novel issues—for instance, consider Icahn’s campaign against AmTrust Financial Services, Inc. where Icahn questioned the applicability of the Delaware Chancery Court’s Kahn v. M&F Worldwide Corp. holding in situations where actions of the acquiror may have been aimed at disenfranchising minority shareholders who acquired shares following the announcement of the sale but before the public announcement of the record date for the vote—but can also proceed on well-defined premises resulting in more legally mundane conclusions.

40 For instance, in Brookfield’s acquisition of Forest City Realty Trust, Mr. Ratner sued to enjoin the target’s shareholder vote a mere 60 hours prior to its scheduled occurrence.
Schattnerv. Papa John’s Intl., Inc., C.A. No. 2018-0542-AGB (Del. Ch. 2019) serves as a reminder of the broad right of directors (not just stockholders) to inspect books and records (including texts and e-mails sent via personal phones and e-mail accounts), and reaffirms the benefits of obtaining contractual waivers of Section 220 demand rights in any settlement that involves giving an activist a board seat.

Third Point’s campaign to control Campbell Soup’s strategic review process is also illustrative. Third Point acquired a position in Campbell’s stock in August of 2018 and proceeded with a public letter campaign, the establishment of its “Refresh Campbell’s” website and the nomination of a competing full slate of directors. Shortly following Campbell’s own subsequent proxy filing, and only about a month prior to the scheduled annual meeting, Third Point sued Campbell’s, accusing its directors of breaching the fiduciary duty of disclosure by, among other things, failing to disclose the incompetence and conflicts of interest of certain of its nominees and requesting that Campbell’s annual meeting be delayed (though not stated, presumably to give Third Point more time to promote its investment thesis and competing slate of directors). The complaint was subsequently made part of a public securities filing by Third Point and covered by major media outlets, including CNBC, Bloomberg and Reuters. Third Point ultimately lost its motion for expedited discovery and expedited hearing for a preliminary injunction, but the court’s decision did not dismiss the lawsuit or bar Third Point from proceeding with broad discovery, deposition and documentary requests, which some commentators viewed as an attempt by Third Point to gather embarrassing documentation that it could use in connection with its proxy fight.41 Although Third Point was unsuccessful in replacing Campbell’s entire board, it did negotiate the right to nominate two directors to Campbell’s board through a settlement reached with Campbell’s later in the year.

Of course, activists are not the only ones doing the litigating. In 2018, the Delaware Chancery Court decided In re PLX Technology Inc. S’holders Litig., C.A. No. 9880-VCL (Del. Ch. 2018). Perhaps most notable for its focus on short-termism as a basis for finding a conflict of interest and its finding that Potomac Capital Partners, as an activist investor, could be liable for aiding and abetting PLX Technology Inc.’s directors’ breach of their fiduciary duties as a result of the actions of its employee on the PLX board, the Chancery Court’s opinion serves as a reminder that (1) fiduciary duties of directors run to a company’s shareholders broadly, not to activists, and boards must conduct themselves accordingly, even in the face of activist pressure, and (2) an activist’s objectives may differ from those of other shareholders and therefore its affiliated director designee(s) may be conflicted in the pursuit of that objective.

In addition, Elon Musk’s recent settlement with the SEC over his take-private tweet, and continued legal trouble over subsequent tweets, provides a reminder that, even under pressure from activists (or, in Mr. Musk’s case, short sellers), care must be taken in public communications regarding present intentions and corporate strategy.

E. COMPANY RESPONSES TO ACTIVISM

Targeted companies utilize a variety of structural and behavioral actions to respond to activist campaigns. Actions taken by target companies in response to campaigns include:

- hiring advisors and taking substantive business steps (such as evaluating strategic alternatives with or without a public announcement, and returning cash to investors through dividends or buybacks);
- governance changes (including those viewed as governance enhancements by shareholders); and
- tactical actions (such as adoption or revision of poison pills, calling of a special meeting, adjourning or postponing meetings, initiation of litigation or changing board size).

More aggressive tactical steps, such as adoption of poison pills and initiation of litigation, remain relatively uncommon during a campaign. Lastly, target board size changes and share buyback announcements in response to activist campaigns decreased sharply below five-year averages.


43 The categorizations of defensive actions taken are derived from categories reported by SharkRepellent.net.

44 Notably, in February, Sinovac Biotech Ltd. became the first company to activate a poison pill in more than a decade. See Reuters, Sinovac Biotech activates ‘poison pill’ defense in rare move (Feb. 22, 2019).
### Actions Taken by Target Companies in Response to Activism

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Act to Increase Shareholder Value (e.g., buybacks or dividends)</td>
<td>8%</td>
<td>21%</td>
<td>12%</td>
<td>15%</td>
<td>10%</td>
<td>13%</td>
</tr>
<tr>
<td>Announce Hiring of Advisors to Evaluate Strategic Alternatives</td>
<td>3%</td>
<td>8%</td>
<td>7%</td>
<td>8%</td>
<td>6%</td>
<td>6%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Governance Changes</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
<th>Five-year average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amend Advance Notice Requirements</td>
<td>2%</td>
<td>4%</td>
<td>3%</td>
<td>2%</td>
<td>2%</td>
<td>3%</td>
</tr>
<tr>
<td>Other Charter/Bylaw Changes</td>
<td>5%</td>
<td>10%</td>
<td>3%</td>
<td>9%</td>
<td>5%</td>
<td>6%</td>
</tr>
<tr>
<td>Corporate Governance Enhancement</td>
<td>1%</td>
<td>3%</td>
<td>4%</td>
<td>2%</td>
<td>2%</td>
<td>2%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Increase Size of Board</td>
<td>5%</td>
<td>17%</td>
<td>10%</td>
<td>10%</td>
<td>6%</td>
<td>10%</td>
</tr>
<tr>
<td>Adopt Poison Pill</td>
<td>7%</td>
<td>1%</td>
<td>2%</td>
<td>3%</td>
<td>2%</td>
<td>3%</td>
</tr>
<tr>
<td>Adjourn Meeting</td>
<td>0%</td>
<td>1%</td>
<td>2%</td>
<td>2%</td>
<td>2%</td>
<td>1%</td>
</tr>
<tr>
<td>Postpone Meeting Date</td>
<td>1%</td>
<td>3%</td>
<td>2%</td>
<td>2%</td>
<td>2%</td>
<td>2%</td>
</tr>
<tr>
<td>Amend Poison Pill</td>
<td>0%</td>
<td>1%</td>
<td>1%</td>
<td>&lt;.5%</td>
<td>1%</td>
<td>1%</td>
</tr>
<tr>
<td>Decrease Size of Board</td>
<td>2%</td>
<td>3%</td>
<td>2%</td>
<td>4%</td>
<td>0%</td>
<td>2%</td>
</tr>
<tr>
<td>Call Special Meeting</td>
<td>1%</td>
<td>1%</td>
<td>1%</td>
<td>1%</td>
<td>2%</td>
<td>1%</td>
</tr>
<tr>
<td>Initiate Litigation</td>
<td>&lt;.5%</td>
<td>1%</td>
<td>0%</td>
<td>2%</td>
<td>1%</td>
<td>1%</td>
</tr>
</tbody>
</table>
Initiating a proxy contest for representation on a company’s board of directors is one of the primary strategies used by activists to achieve their campaign objectives. Defending against a proxy contest requires a public company to expend considerable time and resources as it undertakes to demonstrate to its shareholders that its director candidates are better positioned to lead the company and the company and the board and management are likely to be subject to repeated attacks throughout the course of the proxy contest. It also requires the company and its management and board to absorb and respond to a steady stream of public criticism. As a result, many companies rationally choose to settle with an activist for limited board representation and a standstill agreement, and accept the risk of prolonged controversy and disruption in the boardroom, rather than taking the risks associated with a public proxy contest (see below under the heading “Settlement Agreements” for a more detailed discussion on settlements). This section analyzes key statistics and trends regarding proxy contests, which may help inform strategies for approaching a potential proxy contest.

However, these overall statistics tell only part of the story, as the decision whether or not to settle in individual cases depends upon the particular facts and circumstances. Moreover, as other statistics provided below demonstrate, the consequences of accepting dissident directors can be profound.

### A. HOW OFTEN ARE PROXY CONTESTS SETTLED?

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Number</th>
<th>Went to Vote</th>
<th>Percentage</th>
<th>Settled/Concessions Made</th>
<th>Percentage</th>
<th>Withdrawn</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>51</td>
<td>17</td>
<td>33%</td>
<td>22</td>
<td>43%</td>
<td>5</td>
<td>10%</td>
</tr>
<tr>
<td>2017</td>
<td>47</td>
<td>17</td>
<td>36%</td>
<td>19</td>
<td>40%</td>
<td>11</td>
<td>23%</td>
</tr>
<tr>
<td>2016</td>
<td>49</td>
<td>15</td>
<td>31%</td>
<td>22</td>
<td>41%</td>
<td>12</td>
<td>25%</td>
</tr>
<tr>
<td>2015</td>
<td>73</td>
<td>26</td>
<td>36%</td>
<td>35</td>
<td>48%</td>
<td>12</td>
<td>16%</td>
</tr>
<tr>
<td>2014</td>
<td>62</td>
<td>14</td>
<td>23%</td>
<td>32</td>
<td>52%</td>
<td>16</td>
<td>26%</td>
</tr>
</tbody>
</table>

45 Percentages for 2018 proxy contests throughout this section may not add up to 100% because the total number of 2018 proxy contests includes proxy contests that are still pending (i.e., campaigns announced in late 2018 for the 2019 proxy season).
The total number of proxy contests has been stable over the past three years, following a significant drop-off in the number of reported proxy contests in 2016. The recent stabilization in terms of the number of proxy contests in a given year likely reflects a trend toward engaging in private discussions with activist investors to resolve their concerns before a potential proxy contest is made public.

### Proxy Contests Settled After the Date of the Definitive Proxy Statement

<table>
<thead>
<tr>
<th>Proxy Contests That Went Definitive</th>
<th>As a Percentage of Total Proxy Contests</th>
<th>Proxy Contests Settled After Definitive Date</th>
<th>As a Percentage of Proxy Contests That Went Definitive</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018 24</td>
<td>47%</td>
<td>6</td>
<td>25%</td>
</tr>
<tr>
<td>2017 24</td>
<td>51%</td>
<td>5</td>
<td>21%</td>
</tr>
<tr>
<td>2016 25</td>
<td>51%</td>
<td>7</td>
<td>28%</td>
</tr>
<tr>
<td>2015 36</td>
<td>49%</td>
<td>5</td>
<td>14%</td>
</tr>
<tr>
<td>2014 23</td>
<td>37%</td>
<td>5</td>
<td>22%</td>
</tr>
</tbody>
</table>

Each year since 2015, roughly half of the proxy contests extended beyond the date that the proxy statements for both sides went “definitive”—in other words, closer in time to the date of the shareholders’ meeting at which directors are elected. Of these, issuers and activists generally settled, on average, one in four contests.

### B. RESULTS OF RECENT PROXY CONTESTS

#### Proxy Contests – Short vs. Control Slate

<table>
<thead>
<tr>
<th>Number of Proxy Contests With Short Slate</th>
<th>Percentage of Proxy Contests With Short Slate</th>
<th>Activist Wins at Least One Board Seat (Short Slate)</th>
<th>Number of Proxy Contests With Control Slate</th>
<th>Percentage of Proxy Contests With Control Slate</th>
<th>Activist Wins at Least One Board Seat (Control Slate)</th>
<th>Activist Wins Majority of Board Seats (Control Slate)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>16</td>
<td>31%</td>
<td>50%</td>
<td>35</td>
<td>69%</td>
<td>46%</td>
</tr>
<tr>
<td>2017</td>
<td>23</td>
<td>49%</td>
<td>52%</td>
<td>24</td>
<td>51%</td>
<td>38%</td>
</tr>
<tr>
<td>2016</td>
<td>13</td>
<td>27%</td>
<td>39%</td>
<td>36</td>
<td>74%</td>
<td>36%</td>
</tr>
<tr>
<td>2015</td>
<td>24</td>
<td>33%</td>
<td>42%</td>
<td>49</td>
<td>67%</td>
<td>39%</td>
</tr>
<tr>
<td>2014</td>
<td>18</td>
<td>29%</td>
<td>67%</td>
<td>44</td>
<td>71%</td>
<td>52%</td>
</tr>
</tbody>
</table>

The percentage of proxy contests involving a control slate, or a slate for a majority of the board seats, has ranged from 51% to 74% from 2014 to 2018. This suggests that, once activists invest in formally commencing a proxy contest, many are not content to merely gain a
seat at the table to influence the direction of the company but rather are seeking the ability to control the direction of the company, or at a minimum are willing to threaten a control attempt in order to gain negotiating leverage. Control slates returned to more typical levels after a sharp decline in the number of control slate contests (as a percentage of total contests) in 2017 as compared to prior years.

Over the last five years, approximately 45% of all proxy contests, control slates or short slates (a slate for a minority of the board seats) resulted in the activist investor obtaining one or more seats on the board. However, for each year in our study, short slate contests are somewhat more successful than control slate contests by this measure.

**Short Slate Contests – Number of Board Seats Sought**

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Short Slate Contests</th>
<th>Dissident Nominates 1 Candidate</th>
<th>Dissident Nominates 2 Candidates</th>
<th>Dissident Nominates &gt;2 Candidates</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>16</td>
<td>5</td>
<td>3</td>
<td>8</td>
</tr>
<tr>
<td>2017</td>
<td>23</td>
<td>2</td>
<td>10</td>
<td>11</td>
</tr>
<tr>
<td>2016</td>
<td>13</td>
<td>5</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td>2015</td>
<td>24</td>
<td>2</td>
<td>13</td>
<td>9</td>
</tr>
<tr>
<td>2014</td>
<td>18</td>
<td>2</td>
<td>6</td>
<td>10</td>
</tr>
</tbody>
</table>

When an activist investor puts forward a short slate of directors, they typically nominate two or more director candidates. Over the past five years, activists have sought multiple board seats in approximately 80% of short slate contests each year on average. In 2018, a greater percentage of short slate contests involved activists seeking only one board seat, but activists still sought multiple board seats in the majority of short slate contests.

---

46 The ability of an activist to launch a campaign for a control slate may be limited by regulatory restrictions in certain industries, such as the financial services industry.

47 The information in this chart is based on data from SharkRepellent.net, and is supplemented with publicly available information. See “Notes on the Scope and Sources of Data Used in This Publication” on page 4.
Proxy Contest Settlement Frequency – Short vs. Control Slate

<table>
<thead>
<tr>
<th></th>
<th>Number of Short Slate Contests</th>
<th>Percentage of Short Slate Contests Settled/Concessions Made</th>
<th>Number of Control Slate Contests</th>
<th>Percentage of Control Slate Contests Settled/Concessions Made</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>16</td>
<td>50%</td>
<td>35</td>
<td>40%</td>
</tr>
<tr>
<td>2017</td>
<td>16</td>
<td>48%</td>
<td>24</td>
<td>33%</td>
</tr>
<tr>
<td>2016</td>
<td>13</td>
<td>31%</td>
<td>36</td>
<td>58%</td>
</tr>
<tr>
<td>2015</td>
<td>24</td>
<td>25%</td>
<td>49</td>
<td>60%</td>
</tr>
<tr>
<td>2014</td>
<td>18</td>
<td>44%</td>
<td>44</td>
<td>54%</td>
</tr>
</tbody>
</table>

For the three years before 2017, when an activist investor put forward a short slate of directors, the issuer and activist investor ended up agreeing to settle the contest before a vote approximately 32% of the time on average. In the past two years the settlement percentage has been significantly higher. In 2017, the settlement percentage jumped to 48%; in 2018, the percentage increased to 50%, the highest percentage in our study. In the context of control slates, for the three years before 2017, the issuer and activist investor agreed to settle the contest before a vote approximately 57% of the time on average. In 2017, however, that percentage dropped to 33% and increased slightly to 40% in 2018. This data does not appear to present a clear trend, either relatively or absolutely.

The inconsistency in the frequency of the pre-vote resolution of proxy contests in the short versus control slate contexts may have a number of explanations. One explanation is that management may be predisposed to settling in the context of a short slate contest because it may be more difficult to justify the monetary and reputational cost of publicly fighting an activist that is seeking only one or two board seats. In contrast, in the control slate context, an issuer may be less likely to be able to settle with the activist on acceptable terms and may be increasingly willing to defend the company’s incumbent directors and strategic direction in a public forum. Issuers’ decisions in these cases have been bolstered by data showing that an issuer is more likely to prevail in a control slate contest than the activist.48

---

48 As shown above, over the past five years, activists have won at least one board seat in roughly 42% of control slate contests per year and have won a majority of board seats in roughly 9% of control slate contests per year over the same period.
Outcome of Proxy Contests That Went to a Vote

<table>
<thead>
<tr>
<th></th>
<th>Won by Issuer</th>
<th>Won by Activist</th>
<th>Vote Split</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>7</td>
<td>8</td>
<td>2</td>
</tr>
<tr>
<td>2017</td>
<td>12</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>2016</td>
<td>12</td>
<td>3</td>
<td>0</td>
</tr>
<tr>
<td>2015</td>
<td>17</td>
<td>7</td>
<td>2</td>
</tr>
<tr>
<td>2014</td>
<td>6</td>
<td>8</td>
<td>0</td>
</tr>
</tbody>
</table>

Of the proxy contests that go all the way to a vote, until recently incumbent board candidates had been increasingly successful in defeating activist investors’ slates of directors. The margin of success for companies began to decline and fell to a five-year low in 2018. The reasons for the companies’ declining success rate vary from campaign to campaign and may result, in part, from an increase in the savviness of activists, improvements in the quality of their director nominees and their increasing appeal to institutional shareholders.

Outcome of Proxy Contests That Went to a Vote – Short vs. Control Slate

<table>
<thead>
<tr>
<th>Short Slate Contests</th>
<th>Control Slate Contests</th>
</tr>
</thead>
<tbody>
<tr>
<td>Won by Issuer</td>
<td>Won by Activist</td>
</tr>
<tr>
<td>2018</td>
<td>33%</td>
</tr>
<tr>
<td>2017</td>
<td>80%</td>
</tr>
<tr>
<td>2016</td>
<td>60%</td>
</tr>
<tr>
<td>2015</td>
<td>67%</td>
</tr>
<tr>
<td>2014</td>
<td>33%</td>
</tr>
</tbody>
</table>

From 2015 to 2017, issuers won short slate contests that went to a vote between 60% and 80% of the time. That success rate for short slate contests dropped to 33% in 2018. One possible explanation for the drop is that activist investors have become more selective when pursuing short slate contests. In addition, the limited success of short slate campaigns in the preceding three years, activists may have become increasingly committed to their short slate campaigns and dedicated the necessary resources to see those campaigns through to the finish line.

Similarly, between 2015 and 2017 incumbent slates of directors experienced a fairly rapid year-over-year increase in their success rate with respect to winning control slate votes. In 2018, however, issuer success in control slate contests hit the lowest rate in five years. Although the activist success rate for control contests stayed the same
in 2017 and 2018, a vote split in 2018 occurred in 14% of control contests.

C. WHAT OCCURS IN THE AFTERMATH OF A PROXY CONTEST?

Company Changes in the Aftermath of a Proxy Contest

<table>
<thead>
<tr>
<th>Year</th>
<th>CEO Change</th>
<th>Merger or Spin-off</th>
<th>Additional Proxy Contests</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>6%</td>
<td>6%</td>
<td>0%</td>
</tr>
<tr>
<td>2017</td>
<td>9%</td>
<td>9%</td>
<td>28%</td>
</tr>
<tr>
<td>2016</td>
<td>7%</td>
<td>14%</td>
<td>21%</td>
</tr>
<tr>
<td>2015</td>
<td>11%</td>
<td>14%</td>
<td>11%</td>
</tr>
<tr>
<td>2014</td>
<td>44%</td>
<td>31%</td>
<td>0%</td>
</tr>
</tbody>
</table>

The conclusion of a proxy contest, regardless of the outcome, is often a precursor to change for the company. In the year or so after a proxy contest, it is not uncommon to see changes to senior management or the board of directors, strategic initiatives such as mergers or spin-offs or the continuation of activist efforts through additional future proxy contests (whether waged by the same or another activist). The table above presents how often certain changes or events occur in the aftermath of all proxy contests that go to a vote. Note that because these changes can take time, the 2017 and 2018 data should be considered in light of the fact that enough time may not have elapsed since each proxy contest concluded for some of these changes to take place. Anecdotally, many practitioners believe the incidence of CEO turnover resulting from activism is actually much higher.

There have been fewer CEO changes and mergers or spin-offs from 2015 to 2018, and the likelihood of additional proxy contests declined. However, changes to the board have increased notably since 2014 and have consistently impacted a majority of the target companies after a proxy contest that went to a vote. Activist funds are now holding investments longer, often up to five years, and focusing initially on operational turnarounds. It is possible that activists have had no choice but to adapt to a longer time frame as companies susceptible to quick fixes have largely disappeared due to preemptive actions by boards and prior activist campaigns. We expect that, if operational and share price targets are not achieved, the push for another solution will become more urgent and be reflected in CEO change or merger/spin-off activity at the same rates as appeared in our data for 2014 and 2015.

Interestingly, the frequency of these types of changes does not seem to depend heavily on the outcome of the contest – that is, whether management or the activist won or the vote was split. This may reflect the fact that activists do not typically withdraw following a contest. They often continue campaigns after a lost vote, many times
successfully. It may also indicate that the issues raised during the course of the contest, including those raised by the activist and those arising in shareholder outreach discussions, can in some cases lead the board and management to conclude that responsive steps should be taken even if the management slate wins.

Lastly, no discussion of the aftermath of activist contests would be complete without pointing out that activists are not always successful in delivering the results promised by their campaigns. A good example (but by no means the only example) of this phenomenon is Trian’s investment at GE.49

This section analyzes the publicly filed settlement agreements that have been reached for activist campaigns announced in 2018 as compared to the prior three years, including the frequency of settlements, the timing of reaching a settlement and the key provisions of settlement agreements.

A. FREQUENCY AND SPEED OF SETTLEMENT AGREEMENTS

The percentage of settlement agreements that have been filed with the SEC for 2018 campaigns to date as compared to the total number of completed activist campaigns increased slightly after decreasing significantly in 2017. This trend was consistent for proxy contests as well as other stockholder campaigns.

<table>
<thead>
<tr>
<th>Settlement Agreements Filed with the SEC</th>
<th>Filed Settlement Agreements for Proxy Contests</th>
<th>Filed Settlement Agreements for Other Stockholder Campaigns</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number</td>
<td>Percentage of Total Completed Campaigns</td>
<td>Number</td>
</tr>
<tr>
<td>-------</td>
<td>----------------------------------------</td>
<td>-------</td>
</tr>
<tr>
<td>2018</td>
<td>45</td>
<td>17%</td>
</tr>
<tr>
<td>2017</td>
<td>38</td>
<td>15%</td>
</tr>
<tr>
<td>2016</td>
<td>66</td>
<td>41%</td>
</tr>
<tr>
<td>2015</td>
<td>81</td>
<td>25%</td>
</tr>
</tbody>
</table>

The speed with which settlement agreements have been reached in 2018 is generally in line with each of the prior three years. For the purposes of these calculations, the time when an activist initiates a campaign is deemed as the time when it makes the first public step towards achieving its goal, either by publishing a letter sent to the company, sending a letter to the other shareholders, filing a Schedule 13D or otherwise publicly announcing its intent to initiate a campaign. Of course, in many cases the company and the activist will have had extensive discussions prior to there being any public knowledge of the campaign, and the first public announcement may come in the form of a finalized settlement agreement between the parties. In some instances, the campaign and settlement were announced on the same day, indicating that pre-settlement discussions occurred in private prior to any public announcement of the campaign. These instances were excluded for purposes of calculating the durations outlined in the
table below, although they represented 24% of the settlements we reviewed for 2018.

<table>
<thead>
<tr>
<th>Time between the Initiation of Campaigns and the Date of the Settlement Agreements</th>
<th>Less than 1 month</th>
<th>1–2 months</th>
<th>2–3 months</th>
<th>3–6 months</th>
<th>6 months or more</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>29%</td>
<td>18%</td>
<td>24%</td>
<td>24%</td>
<td>6%</td>
</tr>
<tr>
<td>2017</td>
<td>33%</td>
<td>17%</td>
<td>11%</td>
<td>33%</td>
<td>6%</td>
</tr>
<tr>
<td>2016</td>
<td>23%</td>
<td>19%</td>
<td>21%</td>
<td>25%</td>
<td>12%</td>
</tr>
<tr>
<td>2015</td>
<td>15%</td>
<td>23%</td>
<td>19%</td>
<td>21%</td>
<td>21%</td>
</tr>
</tbody>
</table>

For the purpose of comparison and review, we have chosen not to examine settlement agreements that are either simple appointment letters without any standstill provisions or confidentiality agreements that do not have customary settlement agreement provisions. In addition, in the past two years, where multiple settlement agreements were filed for the same campaign, either because there were multiple activists or because one activist launched campaigns against several affiliates, we limited our review to one settlement agreement.

**B. NOMINATION PROVISIONS AND MINIMUM SHAREHOLDING PROVISIONS**

The majority of settlement agreements relating to 2018 activist campaigns provide for the appointment of a director to the board. The remaining agreements either provide for the nomination of a director candidate or some other arrangement, such as the appointment of an activist as a board observer. A plurality of 35% of settlement agreements reviewed provide for the nomination and/or appointment of two directors to the board, while 15% of agreements cover four or more directors. Compared to 2017, fewer of the agreements that provide for the nomination and/or appointment of new directors are limited to a single director, with notable increases in the proportion of settlements covering two or three directors.

---

50 2018 data for longer-term periods is likely artificially low, because the data includes only completed campaigns, and long-running campaigns announced in mid-2017 will not yet have been completed. This played out in our January 2018 analysis of settlement agreements where we reported that 0% of 2017 settlement agreements had been reached in six months or more year-to-date. Now that more agreements have been reported, this number is up to 6%. We would expect a similar increase in the 2018 numbers.
The appointment of one or more new directors pursuant to a settlement agreement led to a board-size change in 70% of 2018 settlement agreements reviewed, up from 49% in 2017. The change in board size was generally an increase to make room for new nominees, but in some cases there were removals from the board in conjunction with the agreements that led to a decrease in board size. Additionally, of the agreements that provide for an increase in board size, several agreements call for the board size to be decreased following the subsequent annual meeting. When agreements do not provide for a board-size increase, the parties often explicitly agree which incumbent directors will resign to make room for the new director.

65% of 2018 settlement agreements reviewed have provisions requiring minimum shareholding of the activists in order to keep the directors nominated by such activists on the board or to nominate replacements if such directors resign or are otherwise unable to serve. This represents a 13-percentage-point increase from 52% of settlement agreements reviewed for 2017. While the exact ownership level varies, minimum shareholding provisions often permit the investor to dispose of around 50% of its holdings at the time of the agreement. Failure to maintain the threshold may result in the nominees being required to resign from the board, the activist losing the right to name a replacement nominee or the termination of the agreement.

C. BOARD SEATS PURSUANT TO SETTLEMENT AGREEMENTS

We further analyzed data from select campaigns by certain prominent activist funds from 2010 to January 2019 that resulted in settlements granting the fund the right to appoint at least one director to the board of the target company. We specifically looked at the frequency
with which these activists chose to have at least one fund insider appointed to the board, as well as the length of time that the longest-serving insider appointed pursuant to a settlement agreement remained on the board. As shown in the chart below, in 58% of the agreements, at least one of the appointed directors in our data set was an insider of the activist fund. Icahn, Pershing Square, Trian and ValueAct appointed an activist insider in over 85% of the settlements reviewed, whereas Elliott, Jana and Land & Buildings chose an insider in 25% or fewer of the settlements; Starboard and Third Point were almost evenly split between insiders and independents. In 53% of the agreements for which the duration of the settlement agreement has run, at least one insider stayed on the board longer than the length of time that the target company was required to appoint and nominate the director pursuant to the settlement agreement. For agreements in which at least one insider remained on the board for longer than the duration provided for by the settlement agreement, the longest-serving insider for each such agreement has served an average of approximately 27 months longer than the period provided for in the agreement. However, that average likely understates the total amount of time activist insiders stay on a target board following the expiration of the settlement period; in two-thirds of the agreements for which insider appointees remained on the board beyond the duration of the settlement agreement, at least one such nominee was still on the board as of January 2019. Furthermore, as of January 2019, in 11% of the agreements in which insiders were appointed, the insider nominees were still serving and the duration of the settlement agreement had not yet lapsed.
D. ONBOARDING OF NEW DIRECTORS

59% of the settlement agreements reviewed for 2018 include provisions providing for committee membership of the directors appointed or nominated under the agreement. Many agreements provide for appointment to specified key committees, while others mandate that any new committee formed in the future contain one or more of the activist’s directors. Additionally, 13% of agreements reviewed require the formation of new board committees, compared to 19% for 2017 and 8% for 2015 and 2016. For example, in the Sempra-Elliot cooperation agreement, Sempra agreed to establish a “LNG and Business Development Committee” with a mandate to work with management and the board to conduct a comprehensive business review of the company. As at Sempra, the new committees are typically dedicated to a topic related to the activist campaign, with examples including the “Finance and Strategy Committee,” “Business Development Committee” and “Operating Improvement Committee.” Where the settlement agreements we reviewed do not provide for committee membership, the agreement either notes that the company must consider the nominee/appointee for committee membership along with other members of the board or is silent on committee membership.

78% of agreements reviewed for 2018 specifically address the topic of information-sharing by the new director with the activist, the same percentage as in 2017. However, in 2018, a lower proportion of agreements expressly permit the sharing of such information, down from 18% to 7%. 46% of agreements subject new directors to the board’s standard policies regarding confidential information, while an additional 26% also involved confidentiality agreements, both of which were up roughly seven percentage points from 2017.

E. STANDSTILL PROVISIONS

Almost every settlement agreement includes a standstill provision, which prohibits activists from engaging in certain activities within a prescribed period of time. The main purpose of the standstill provision is to restrict the activist from initiating or participating in any further campaigns. The standstill period generally runs from the date of the settlement agreement until a date tied to the time when the director nominated by the activist is no longer required to be nominated to serve on the board (or earlier upon a material breach by the company of provisions in the settlement agreement).

The following table lists the types of activities typically restricted by the standstill provisions and the frequency of their inclusion in 2018.
<table>
<thead>
<tr>
<th>% of 2018 Agreements</th>
<th>Activities Prohibited</th>
</tr>
</thead>
</table>
| 91%  
Soliciting proxies or consents. | Prohibits activists from making, engaging in or in any way participating in, directly or indirectly, any “solicitation” of proxies or consents to vote, or advising, encouraging or influencing any person with respect to the voting of any securities of the company. |
| 89%  
Publicly disparaging the company or its directors or officers. | Prohibits activists from disparaging or negatively commenting on the company or its affiliates or any of their respective officers or directors, including the company’s corporate strategy, business, corporate activities, board or management. Of the settlement agreements we reviewed, 90% include a mutual non-disparagement clause that also prohibits the company from publicly disparaging the activists. |
| 89%  
Seeking board additions or removals. | Prohibits activists from seeking to elect or remove any directors or otherwise seeking representation on the board. |
| 87%  
Forming a group or a voting trust or entering into a voting agreement. | Prohibits activists from forming or participating in any Section 13(d) “group” with any persons who are not their affiliates with respect to any securities of the company or seeking to deposit any securities of the company in any voting trust, or subjecting any such securities to any voting agreements (other than any such voting trust, arrangement or agreement solely among the activists and their affiliates). |
| 85%  
Presenting a shareholder proposal. | Prohibits activists from making any proposal at any annual or special meeting of the shareholders. |
| 83%  
Calling shareholder meetings or referendums. | Prohibits activists from calling or seeking the company or any other person to call any meeting of shareholders, as well as action by written consent, or conducting a referendum of shareholders. |
<table>
<thead>
<tr>
<th>% of 2018 Agreements</th>
<th>Activities Prohibited</th>
</tr>
</thead>
<tbody>
<tr>
<td>72%</td>
<td><strong>Seeking amendments or waivers from the standstill or challenging validity of the standstill.</strong> Prohibits activists from publicly requesting any waiver of or amendment to the standstill provision or contesting the validity thereof. A majority of the settlement agreements include an exception that such actions could be pursued through non-public communications with the company that would not be reasonably determined to trigger public disclosure obligations.</td>
</tr>
<tr>
<td>74%</td>
<td><strong>Entering into third-party agreements that go against the settlement agreement.</strong> Prohibits activists from entering into any discussions, negotiations, agreements or understandings with any third party with respect to any activities restricted by the standstill provision.</td>
</tr>
<tr>
<td>70%</td>
<td><strong>Seeking extraordinary transactions not recommended by the board.</strong> Prohibits activists from seeking, facilitating or participating in “extraordinary transactions” not recommended by the board. The term “extraordinary transactions” is generally defined to include any tender or exchange offer, merger, consolidation, acquisition, scheme, arrangement, business combination, recapitalization, reorganization, sale or acquisition of assets, liquidation, dissolution or other extraordinary transaction involving the company. Some settlement agreements include an exception that the activists could still tender their shares into any tender or exchange offer or vote their shares with respect to any extraordinary transactions. The prohibition sometimes extends to making public communications in opposition to the extraordinary transactions approved by the board.</td>
</tr>
<tr>
<td>65%</td>
<td><strong>Bringing litigation or other proceedings (other than to enforce the settlement agreement).</strong> Prohibits activists from instituting or joining any litigation, arbitration or other proceeding (including any derivative action) against the company or its directors or officers other than to enforce the provisions of the settlement agreement. Many settlement agreements also include exceptions for counterclaims with respect to any proceeding initiated by the company against the activists, exercise of statutory appraisal rights or responding to or complying with a validly issued legal process.</td>
</tr>
<tr>
<td>% of 2018 Agreements</td>
<td>Activities Prohibited</td>
</tr>
<tr>
<td>---------------------</td>
<td>-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>61%</td>
<td><strong>Requesting a shareholder list or books and records.</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Seeking to control or influence the company or the management.</strong> While many settlement agreements simply provide for a flat prohibition on any actions designed to control or influence the company or management, some settlement agreements specify the types of activities that are prohibited, including any proposal to change the composition of the board, any material change in the capitalization, stock repurchase programs or dividend policy, any other material change in the company's management, business or corporate structure, amendments to the certificate of incorporation or bylaws, causing a class of securities of the company to be delisted from any securities exchange or become eligible for termination of registration pursuant to Section 12(g)(4) of the Exchange Act.</td>
</tr>
<tr>
<td>59%</td>
<td><strong>Publicly announcing intent to go against the settlement agreement.</strong> Prohibits activists from making any public disclosure, announcement or statement regarding any intent, purpose, plan or proposal that is inconsistent with the standstill provisions.</td>
</tr>
<tr>
<td>55%</td>
<td><strong>Acquiring more shares.</strong> Prohibits activists from acquiring, offering to acquire or causing to be acquired beneficial ownership of any securities of the company such that immediately following such transaction the activists would have beneficial ownership of securities exceeding a certain prescribed limit. Settlement agreements sometimes clarify that exceeding the limit as a result of share repurchases or other company actions that reduce the number of outstanding shares should not be counted as a breach of this clause.</td>
</tr>
</tbody>
</table>
### % of 2018 Agreements

<table>
<thead>
<tr>
<th>Activities Prohibited</th>
<th>% of Agreements</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transferring shares to a third party.</td>
<td>41%</td>
</tr>
<tr>
<td>Prohibits transfers of the company’s securities to a third party that would result in such third party having aggregate beneficial ownership of more than a certain percentage. Many settlement agreements carve out certain parties from this restriction, such as parties to the settlement agreement, directors and officers of the company and/or affiliates of the company. A small number of settlement agreements also prohibit any purchase, sale or grant of any option, warrant, convertible security, stock appreciation right or other similar right.</td>
<td></td>
</tr>
<tr>
<td>Short selling.</td>
<td>17%</td>
</tr>
<tr>
<td>Prohibits activists from engaging in short selling of the company’s securities.</td>
<td></td>
</tr>
</tbody>
</table>

Once again, the frequency of activities prohibited in standstill agreements remained relatively stable from 2017 to 2018, with certain notable exceptions. Last year, we noted an increase in prohibitions on short selling from 17% across 2015 and 2016 to 32% in 2017 and a corresponding drop in prohibitions on transfers of shares to third parties from 46% to 29%. That trend reversed in 2018, with short selling prohibitions back down to 17% and prohibitions on transferring shares to third parties back up to 41%, both in alignment with 2015/2016 frequencies. However, as discussed above, there was a corresponding 13-percentage-point increase in settlement agreements containing minimum share ownership levels. Additionally, several agreements that were publicly filed in 2018 specifically prohibit the investors from buying or selling voting rights decoupled from the underlying securities.

Prohibitions on activists seeking extraordinary transactions not recommended by the board remain the norm but have declined over the past few years. Such provisions were found in 70% of agreements reviewed for 2018, down from 84% in 2017 and 96% across 2015 and 2016.

Additionally, there was a 22% decrease (from 94% in 2017 to 72% in 2018) in provisions prohibiting the activist from publicly seeking amendments or waivers from the standstill. The majority of agreements containing such a prohibition include an exception if such request is made privately to the company’s directors or officers.

### F. VOTING AGREEMENTS

83% of the 2018 settlement agreements reviewed include a provision requiring the activists to vote their shares in a prescribed manner within the standstill period compared to 94% of settlement agreements in 2017. 7% of the settlement agreements simply require the activist to vote for all the director candidates nominated by the
board, and 2% of the settlement agreements require the activists to vote in accordance with all board recommendations. The remaining 74% of settlement agreements either specify proposals for which the activists must vote (such as ratification of the appointment of an auditor, “say-on-pay” proposals, proposals regarding equity incentive plans, specific transactions, etc.) or include exceptions permitting activists to vote in their own discretion on certain proposals.

One of the most common exceptions to the voting agreement provision is when a board recommendation differs from that of the proxy advisors ISS and/or Glass Lewis. This exception appears in 39% of settlement agreements reviewed for 2018, marking an upward trend from 26% in 2017 and 22% in the prior two years. This exception takes several forms. In some cases investors are permitted to vote against the board recommendation if either ISS or Glass Lewis makes a recommendation differing from that of the board with respect to a proposal, while other times both ISS and Glass Lewis must make such a differing recommendation. Some agreements also limit the exception to ISS recommendations only. Additionally, some agreements limit the ISS/Glass Lewis exception to only specified matters, such as “say-on-pay” proposals, requiring the investor to support most or all other board recommendations notwithstanding an ISS/Glass Lewis recommendation to the contrary.

Other exceptions include extraordinary transactions (e.g., mergers or liquidations), amendments to the company’s articles of incorporation, stock issuances and compensation plans.

<table>
<thead>
<tr>
<th>Voting Provisions</th>
<th>2018 Percentage</th>
<th>2017 Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>All board recommendations</td>
<td>2%</td>
<td>10%</td>
</tr>
<tr>
<td>Specific board recommendations or exceptions</td>
<td>74%</td>
<td>68%</td>
</tr>
<tr>
<td>The board slate only</td>
<td>7%</td>
<td>16%</td>
</tr>
<tr>
<td>No voting provision</td>
<td>17%</td>
<td>6%</td>
</tr>
<tr>
<td>ISS/Glass Lewis exception to voting provision</td>
<td>39%</td>
<td>26%</td>
</tr>
</tbody>
</table>

G. EXPENSE REIMBURSEMENT

52% of the settlement agreements reviewed for 2018 require the issuer to pay some portion of the activist’s expenses, with the remaining 48% either silent on the topic or expressly stating that each party shall pay for its own expenses. While the percentage of agreements providing for expense reimbursement in 2018 was consistent with 2017, the distribution of expense reimbursement caps changed. In
2018, there was a substantial increase in the percentage of settlements in which the company reimbursed expenses up to a cap of $100,000 to $500,000, up from 13% to 24%, and a corresponding decrease in the percentage of settlements with an expense reimbursement cap of $500,000 or more, down from 16% to 7%. These changes bring 2018 back in line with reimbursement caps observed in 2015 and 2016 (22% and 6%, respectively). According to Activist Insight Online, the average settlement reimbursement amount in 2018 was up to $431,831 from $157,000 in 2017. Activist Insight Online attributes much of this increase to the higher number of reimbursements from mid-cap and large-cap companies, although this increase was also impacted by the presence of three multimillion-dollar reimbursements in 2018: (1) Newell Brands-Starboard ($2 million cap); (2) Innovia-Sarissa Group ($2.7 million cap) and (3) Wynn Resorts-Elaine Wynn ($5 million cap). In comparison, 2017 settlements with expense reimbursement caps above $500,000 or more largely had caps between $500,000 and $1,000,000.

Additionally, there were two settlements in 2018 requiring the issuer to reimburse expenses without disclosing a cap—one such agreement references an undisclosed cap privately agreed upon by the parties while the other provides for the reimbursement of “reasonable” fees.

<table>
<thead>
<tr>
<th>Expense Reimbursement</th>
<th>2018 Percentage</th>
<th>2017 Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Each party pays for its own expenses</td>
<td>48%</td>
<td>45%</td>
</tr>
<tr>
<td>Cap of less than $100,000</td>
<td>17%</td>
<td>26%</td>
</tr>
<tr>
<td>Cap of $100,000 to $500,000</td>
<td>24%</td>
<td>13%</td>
</tr>
<tr>
<td>Cap of $500,000 or more</td>
<td>7%</td>
<td>16%</td>
</tr>
<tr>
<td>Others (including no cap)</td>
<td>4%</td>
<td>0%</td>
</tr>
</tbody>
</table>
As much as activism has matured and there has been a proliferation of literature on the topic in the past couple of years, there are still a few areas that we think merit further study. These, however, are beyond the scope of our analysis as they require economic or statistical analysis or other data that is not readily available to us at this time.

1. The Correlation between Stock Drops and Activism

When clients ask how they can avoid having an activist come into their stock, we always tell them that they should focus on having good performance, high returns and a healthy stock price. This is easier said than done, of course. But we do think it would be very interesting to study the extent to which issuers’ stock drops correlate with activism and, if they do correlate, what kinds of patterns emerge. Is a single quarter downturn sufficient to attract an activist or must the drop be sustained over multiple quarters? How far does the stock have to drop before an activist will become interested? Is an activist more likely to emerge following a significant one-time adverse event or a persistent operational or financial performance issue? Is the extent of the drop relative to peers a more relevant metric than an absolute drop?

2. ISS’s and Glass Lewis’s Influence in Activism Contests

There was continued discussion in 2018 about potential reforms that could impact the activism landscape, including universal ballots, 13D timing, the SEC’s Proxy Roundtable and regulation of proxy advisors to name a few. The proxy advisor issue in particular has garnered a lot of attention in relation to activism in the past. Preliminary research suggests that passive investors are strongly aligned with ISS on management proposals.\textsuperscript{51} One recent study of 713 institutional investors in 2017 found that proxy contests receive 73% more institutional investor support when ISS supports the measure and 64% more support when Glass Lewis supports the measure, but we have not identified any comprehensive studies addressing the true extent of the correlation between ISS recommendations and voting behaviors in activism contests. Moreover, much of the available data focuses on the voting records of the largest institutional investors, whose behaviors may not be representative of smaller funds who do not have in-house research departments and therefore may be more likely to rely on proxy advisor recommendations.

Another interesting area for further study would be to analyze the extent of any correlations between proxy advisor score card results and

activism vulnerability. For example, are companies that have high ISS QualityScores more likely to enjoy a safe harbor from activists because the activists are forced to make economic arguments rather than governance arguments? This suggestion for further analysis presupposes that ISS and Glass Lewis are “leading indicators” of the latest waves of governance reforms, but in reality a better comparison might be to Council of Institutional Investor policies or to the voting guidelines of the largest index funds.

3. Activism as Export

Our study focuses entirely on activism directed at U.S. issuers, but much of the headline-grabbing 2018 activism actually targeted non-U.S. issuers.52 One area for further study would be to try to assess whether the non-U.S. issuers targeted by activists have any common attributes – size, jurisdiction of formation, regulators, etc. Taking it a step further, it would also be very interesting to collect data to assess what strategies appeared to be most successful outside of the U.S. (both on the activist side and the issuer side). There are European activism studies available,53 but until recently the number of data points were probably too limited to draw any definitive conclusions about statistical correlations.

*   *   *

The 2018 activism landscape, which has been highlighted by a record number of first-time activists launching campaigns, increased success of activist nominees at obtaining board seats (largely through settlements) and an increased focus on M&A, suggests that activism will continue to be an important consideration for companies in 2019. Additional topics of activist and institutional investor focus, such as ESP and governance-related shareholder proposals, will be revisited in our 2019 Proxy Season Review.

*   *   *

Contacts

Palo Alto
Sarah P. Payne
+1-650-461-5669
paynesa@sullcrom.com

Melbourne & Sydney
Waldo D. Jones Jr.
Melbourne
+61-3-9635-1508
Sydney
+61-2-8227-6702
jonesw@sullcrom.com

London
John Horsfield-Bradbury
+44-20-7959-8491
horsfieldbradburyj@sullcrom.com

Tokyo
Keiji Hatano
+81-3-3213-6171
hatanok@sullcrom.com

Jeremy Kutner
+44-20-7959-8484
kutnerj@sullcrom.com

Hong Kong
Garth W. Bray
+852-2826-8691
brayg@sullcrom.com

Evan S. Simpson
+44-20-7959-8426
simpsone@sullcrom.com

Michael G. DeSombre
+852-2826-8696
desombrem@sullcrom.com

Paris
Olivier de Vilmorin
+33-1-7304-5895
devilmorino@sullcrom.com

Chun Wei
+852-2826-8666
weic@sullcrom.com

William D. Torchiana
+33-1-7304-5890
torchianaw@sullcrom.com

Beijing
Gwen Wong
+86-10-5923-5967
wonggw@sullcrom.com

Frankfurt
Carsten Berrar
+49-69-4272-5506
berrarc@sullcrom.com

Krystian Czerniecki
+49-69-4272-5525
czernieckik@sullcrom.com