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**Proxy Access: When Shareholders Nominate directors**

***By Adrian Chan***

Though directors are elected by shareholders, the nominations for their election are usually made by the board of directors following an internal nomination process that often includes a nominating committee-led search for suitable candidates.

However, a view is emerging, especially in the US, that this process does not result in the best set of directors, and that some boards acting out of self-interest can entrench themselves.

**US developments**

In the US, companies mail proxy cards to investors ahead of shareholder meetings that usually list only the board's slate of nominees for board seats. This is now slowly changing.

In March, Bank of America announced amendments to its bylaws that would allow a group of up to 20 shareholders to nominate up to 20 per cent of its directors provided they have owned more than 3 per cent of the company's stock for at least three years.

A growing list of US companies is adopting this "three and three" approach as part of a director-nomination reform known as "proxy access". With proxy access, longer-term shareholders can more easily nominate their own candidates on a company's proxy card. This lets investors avoid the cost of sending out their own proxy cards or requisitions when they are dissatisfied with a corporate board and want to run their own candidates as directors. Even after nomination by proxy access, a majority of shareholders must still elect the shareholder nominee(s) at the shareholder meeting, preventing the election of directors not supported by most shareholders.

General Electric, Hewlett-Packard and Verizon Communications have already changed their corporate governance rules to reflect this new process.

There have been, however, some pushbacks against proxy access, most notably by the likes of Whole Foods, Peabody Energy and Arch Coal.

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The stakes are high. On the other side of the battle-line, institutional investors such as pension and hedge funds have warned that they may recommend shareholders to vote against management's preferred directors if companies ignore shareholder nominations by proxy access.

New York City Comptroller Scott Stringer has described the proxy access debate as gaining "global momentum" and as the governance "issue for 2015 and beyond".

**Proxy access or not?**

Proponents argue that proxy access makes boards more accountable and less insular as all shareholders get to decide on the best candidates from among the nominees proposed by management and shareholders. In turn, fair and transparent board elections help raise market capitalisation and improve returns. Boards become more responsive to shareholders. They are more vigilant in their oversight of companies.

At least, that's the theory.

Opponents of proxy access are concerned that activist investors could buy stakes in companies to hijack the election process or pursue special interest agendas. They worry, too, about the cost of proxy access, while remaining unconvinced that it will improve either company or board performance. Still others argue that shareholders might propose directors who lack adequate background or experience for the role.

**The Singapore situation**

Most developed markets already feature some version or another of proxy access, but even then, its use is not widespread. A 2014 CFA Institute study showed that in Canada, the United Kingdom and Australia, investors used proxy access to nominate directors fewer than 10 times a year.

In a sense, Singapore already has proxy access. The Companies Act permits two or more shareholders holding at least 10 per cent of the issued shares to call for a shareholders' meeting at the cost of the company. Furthermore, shareholders owning at least 5 per cent of a company's shares (or not less than 100 shareholders holding a paid-up value of at least S\$500) may, at their cost, propose a resolution for voting at a general meeting. This means that shareholders can, if they meet these shareholding tests, effectively nominate their own directors for election.

However, these minimum requirements are not easily met in large capitalised companies. This explains the interest in the American "three and three" approach which, of course, sets a lower threshold for shareholder activism.

This is not to say that Singapore has not seen its fair share of shareholder-led appointments and removals of directors. For example, as recently as April, a group of investors that owned 16 per cent of Singapore-listed Cedar Strategic Holdings called a shareholders' meeting and successfully removed four directors and appointed three of their nominees to the board.

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So is there any need for minority shareholders in Singapore to have another avenue to put their nominees up for election at annual general meetings? Given that there are minimum ownership thresholds in both shareholdings and duration of ownership and limits on the number of directors nominated by shareholders, perhaps it is timely to reassess whether the market here is ready for a more liberal proxy access process.

Though not yet as live an issue in Singapore as it is in the US, proxy access reform is, at its core, a movement to empower shareholders. As such, it is a stark reminder to local boards and nominating committees that they should assess, on an ongoing basis, the broader issues of board composition, tenure, refreshment, and shareholder engagement and outreach.

*The writer is the first vice-chairman of the Singapore Institute of Directors. This article first appeared in BTInvest,*

<http://www.btinvest.com.sg/specials/boardroom/proxy-access-when-shareholders-nominate-directors/>