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ACCESS TO THE CORPORATE PROXY MACHINERY

Melvin Aron Eisenberg *

After sketching the legal and economic background of proxy voting, Professor Eisenberg reexamines the direct authorities and general principles of corporate law concerning access to corporate proxy machinery. He analyzes the conditions under which, and the extent to which, management and shareholders can utilize the proxy machinery in connection with both election and nonelection matters. In particular, he develops the point that the shareholders are afforded significantly wider access under state corporate law than has commonly been assumed.

[A] large portion of that legal opinion which has passed current for law, falls within the description of "law taken for granted." If a statistical table of legal propositions should be drawn out, and the first column headed "Law by Statute," and the second "Law by Decision;" a third column, under the heading of "Law taken for granted," would comprise as much matter as both the others combined. But . . . the mere statement and restatement of a doctrine,—the mere repetition of the cantilena of lawyers, cannot make it law, unless it can be traced to some competent authority, . . . if it be irreconcilable to some clear legal principle.

Lord Denman ‡

SHAREHOLDERS elect directors and determine fundamental corporate actions; this is an essential aspect of the received legal model of the corporation,¹ but one which does not always

† Copyright 1970 by Melvin Aron Eisenberg. This article is the second in a series of articles on the allocation of legal powers within the modern corporation. See Eisenberg, The Legal Roles of Shareholders and Management in Modern Corporate Decisionmaking, 57 CALIF. L. REV. 1 (1969).


correspond to reality. In an article published last year I showed that the interests and expectations of shareholders in the modern corporation seem to have been significantly underestimated due to the uncritical acceptance of a fallacy and a myth: the fallacy that the key element in determining such interests and expectations is the total number of shareholders in a given corporation, rather than the extent to which holdings are concentrated; and the myth that corporations like AT&T, whose shareholdings are very highly dispersed, are representative in this respect of the entire class of corporations, or even of the subclass of publicly held corporations. Nevertheless, in any number of publicly held corporations de facto control over election of directors and fundamental corporate actions does reside with management rather than with shareholders.

What accounts for this phenomenon? In large part it is undoubtedly due to economic realities. For example, if management is performing at a level between good and excellent, it may make no sense to replace it or to disagree with its recommendations. Even where management's performance is less than good, no better alternative may be available. And of course management itself may hold or represent a large block of stock.

But management control over elections and fundamental actions may sometimes result not from economic realities, but from legal rules, or at least from supposed legal rules. In particular, it is generally assumed that the legal rules governing the proxy system help insure management control by giving management virtually exclusive and practically unlimited access to the corporate proxy machinery.

If this assumption is correct, it would be of utmost significance. It is well known that proxy voting has become the dominant mode of shareholder decisionmaking in publicly held corporations. There are a number of reasons for this. Shareholders in such corporations are often geographically dispersed, so that a given shareholder may not live near the site of the meeting. Shareholders often have some principal business other than investing, so that a given shareholding may not represent a substantial proportion of a shareholder's total wealth. And whether a shareholder supports or opposes the matters scheduled for action at a meeting, he may not wish to speak on the issues. Physical

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2 Eisenberg, The Legal Roles of Shareholders and Management in Modern Corporate Decisionmaking, 57 Calif. L. Rev. 1, 60–61 (1969).
3 See id. at 33–53.
attendance at a shareholders' meeting is normally an uneconomical use of a shareholder's time when he can vote by proxy. 5

A natural outgrowth of the preference for proxy voting is proxy solicitation—the process of systematically contacting shareholders and urging them to execute and return proxy cards which authorize named proxies to cast the shareholder's votes, either in a manner designated in the proxy card or according to the proxies' discretion. If a substantial proportion of the corporation's stock is controlled by a few persons, or if the total number of shareholders is relatively small, a solicitation can, absent legal regulation, be relatively casual—a few dozen phone calls or letters may suffice. If not, a more elaborate solicitation is required. This would normally include a widespread mailing of written materials to shareholders, and follow-up letters and phone calls to those who do not respond. In many cases, professional proxy solicitors may be hired to do the follow-up, adding significantly to total expense. 6 Finally, solicitations in respect of certain securities are subject to the SEC's Proxy Rules 7 and therefore entail the additional expense of preparation or screening by counsel.

Persons who solicit proxies may pay these expenses out of their own pocket. However, they prefer to shift the financial burden of a solicitation to the corporation itself by using corporate funds to pay for printing, lawyers, professional proxy solicitors and other expenses, and by using corporate personnel and facilities to make mailings, phone calls, and personal contacts—in short, by using the complex of men, money, and facilities known as the corporate proxy machinery. The questions then arise: Who can make use of the corporate proxy machinery? Under what circumstances can such use be made?

Given the dominance of proxy voting, if the common assumption that the law gives management virtually exclusive access to this machinery is correct, obviously the law itself would contribute substantially toward entrenching management control of

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6 Following conventional usage, the term "proxy" will be used in this article to refer to: (a) a person appointed by a shareholder to appear at a meeting and cast the shareholder's vote, and (b) the form (usually a printed card) in which such an appointment is embodied.


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publicly held corporations. Examination of the authorities, however, reveals that this assumption has little or no direct support. State corporation statutes generally are silent on questions of proxy regulation in general and access in particular. At common law a shareholder could not vote by proxy unless the corporation's certificate or bylaws expressly so provided. This rule was early changed by the corporate statutes, and today every state permits proxy voting even in the absence of certificate or bylaw provision. But the purpose of the relevant statutory provisions was merely to empower proxy voting, not to regulate its mechanics, and while the proxy system grew in significance and complexity, the corporate statutes failed to grow with it. By and large, state corporate statutes do not even recognize the existence of proxy solicitation, let alone regulate it.

Parts of the gap left by the state statutes have been filled by other sources. Case law has addressed itself in a general and somewhat unsatisfactory way to certain problems of management access, and also to problems arising out of misleading statements in proxy solicitation materials, but it is extremely sparse on

9 Id. at 46–48.
11 See 2 id. at 866; cf. N. Lattin, R. Jennings & R. Buxbaum, Corporations: Cases and Materials 454 (4th ed. 1968); Stifel, Shareholder Proxy Fight Expenses, 8 Clev.-Mar. L. Rev. 339 (1959). For a discussion of solicitation abuses under state law, see Note, The SEC Proxy Rules and Shareholder Participation in Management, 53 Harv. L. Rev. 1165 (1940). There are limited exceptions. Prominent are Cal. Corp. Code § 3637 (West 1955) and § 25148 (West Supp. 1969). Section 3637 provides that shareholders who are solicited to approve certain types of certificate amendments must be given a concise summary of the proposed amendment and the changes in shareholder rights which the amendment will effect. However, it adds that “failure to comply with this section does not invalidate the amendment.” Section 25148 authorizes the California Commissioner of Corporations to require a proxy statement in certain cases by rule or by order. See generally H. Marx & R. Volk, Practice Under the California Corporate Securities Law of 1968, at 239–40, 326 (1969).

Under the 1964 amendments to the Securities Exchange Act, securities issued by an insurance company may be exempt from registration under the Act if, among other things, “[s]uch insurance company is subject to [proxy] regulation by its domiciliary State . . . and such regulation conforms to that prescribed by the National Association of Insurance Commissioners.” Securities Exchange Act of 1934, § 12 (g)(2)(G)(ii), 15 U.S.C. § 78l (g)(2)(G)(ii) (1964). In order to permit domiciled insurance companies to qualify for exemption, most states now regulate the solicitation of proxies by such companies, either by statute or by statutorily authorized rules issued by the commission of insurance. See 5 Loss 2752–53 (Supp. 1969).

12 See pp. 1494–99 infra.
problems of shareholder access. In contrast to the case law, the Proxy Rules issued by the SEC under section 14 of the Securities Exchange Act of 1934 fill large parts of the gap in a highly elaborate way. Indeed, the presence of these rules and the central administrative mechanism for enforcing them may account in part for the inaction of state legislatures in this area. But, even the Proxy Rules leave substantial lacunae. They do not extend to all proxy solicitations, but only those in respect to certain securities — generally speaking, securities which are either listed on a national securities exchange, or are equity securities issued by a corporation with assets of more than one million dollars and held by 500 or more shareholders. Furthermore, the Proxy Rules reflect the original philosophy of the securities legislation, which was to require disclosure of relevant information and to prohibit the use of false information, rather than to control the internal government of corporations. Accordingly, the Proxy Rules deal elaborately with the information that must accompany a proxy solicitation, but only tangentially with access to the corporate proxy machinery.

In the absence of direct authority, questions of access to the corporate proxy machinery must be decided by the application of general corporate principles, elaborated in light of those considerations of policy and practicability relevant to the particular question. The purpose of this article is to reconsider the direct authorities, and to identify, elaborate, and apply the relevant general principles applicable to such questions, with a view toward delineating the legal rules by which such questions should be governed. Two general propositions will underlie much of the discussion, and should therefore be stated briefly at the outset. First, the corporate proxy machinery is just that — corporate
proxy machinery, constructed of corporate assets, and fueled with corporate funds. Thus, it cannot be appropriated to personal ends; if set in motion at all, it must be operated in a neutral manner. Second, the proxy system has developed to the point where it not merely leads up to but supplants the shareholders’ meeting for most substantive purposes and, in some respects, for formal purposes as well. 18 “[R]ealistically the solicitation of proxies is today the stockholders’ meeting.” 20 Typically a shareholder in a publicly held corporation will make his voting decision at some point during the solicitation process rather than at the meeting and thus, insofar as his decision is based upon persuasion, the persuasion will occur during the solicitation process rather than at the meeting. This expectation informs all aspects of shareholder decisionmaking: beginning with the proxy card, which is normally in the form of a ballot; 20 proceeding through Proxy Rule 14a–4, which prohibits, except in very limited cases, the distribution of proxy cards which give the proxy holder unfettered discretionary authority to vote at the meeting; 21 and ending at a meeting room which is normally too small to seat more than a tiny fraction of the corporation’s shareholders. Because of this shift in the locus of shareholder decisionmaking, at least some of the principles and rules developed to govern the process known as shareholders’ meetings should now be applied to the process known as proxy solicitation.

I. Access to the Corporate Proxy Machinery in Connection with the Election of Directors

A. Management Access

It might seem surprising that management, in the person of the board, should have any access at all to the corporate proxy machinery for election of directors. A directorship is after all a position of value: it normally pays a fee; it confers upon the holder a share in the control of a business enterprise; it may shore up a lucrative employment position (in the case of an


19 Bernstein & Fisher, supra note 18, at 227.

20 See Proxy Rule 14a–4(a), (b), 17 C.F.R. §§ 240.14a–4(a), (b) (1969).

21 See Proxy Rule 14a–4(b)(i), (c)–(e), 17 C.F.R. §§ 240.14a–4(b)(i), (c)–(e) (1969).
inside director), or provide a preferential track to business dealing with the corporation (in the case of an outside director); and it carries prestige in the managerial peer group. Thus, to permit incumbent directors to use the corporate proxy machinery to help them gain a new term of office might appear to be a blatant appropriation of corporate assets to personal ends. So Professor Brudney has observed that "[s]trict fiduciary standards would categorically preclude insiders from spending corporate funds to perpetuate their power . . . ."

Nor is the only problem that of fiduciary standards. Corporate organs can act only within their authority; but what authority does the board have to use the corporate proxy machinery in connection with the election of the board? Certainly this is not a specific board function. On the contrary, under the corporate statutes the power to elect the board is vested exclusively in the shareholders. While the statutes normally give the board a broad residual power to manage the business of the corporation, recommendations by the board that the shareholders reelect its members hardly seem to fall within the scope of that provision, particularly considering that the election of the board is assigned specifically to the shareholders.

Consistent with these principles, the courts have regularly said that the board cannot use the corporate proxy machinery for the purpose of perpetuating itself in office. Of course the board can use that machinery to call a shareholders' meeting, to produce a quorum, and presumably to prepare and distribute any materials required by law. Such a use neither violates strict fiduciary

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22 See The Director Looks at His Job 146-47 (C. Brown & E. Smith eds. 1957); G. Washington & V. Rothschild, Compensating the Corporate Executive 255-60 (3d ed. 1962).
25 The significance of the eight corporate statutes cited, and the extent to which they may be viewed as representative of corporate statutory law as a whole, are discussed in Eisenberg, supra note 2, at 60-61.
28 See Hall v. Trans-Lux Daylight Picture Screen Corp., 20 Del. Ch. 78, 82-83,
standards nor exceeds the board’s authority. The board, however, will normally wish to do more. At a minimum, it will want to designate its members as candidates in the corporate proxy materials. The incremental expenditures involved in this practice are minimal, and when the election is uncontested it probably presents no serious problem. If the election is contested, however, the members of the board will want to use the corporate proxy machinery to wage an active campaign on their own behalf. To the question whether this is permissible in the face of the rule that the board cannot use the corporate proxy machinery to perpetuate itself in office, the courts have answered, “yes,” provided that (1) the contest involves a policy issue, (2) the expenses involved are for the purpose of informing the shareholders concerning the policy issue, and (3) the expenses are reasonable.

Superficially, use of this test enables the courts to stay within a rationale that the board can use the corporate proxy machinery when, but only when, it is acting within its authority and not violating normal fiduciary standards. Surely, the argument runs, the board has authority to make recommendations to the shareholders on issues of corporate policy, and surely making such recommendations does not violate the board’s fiduciary duty.

But despite its surface appeal, this test is fundamentally defective. In terms of authority, the rationale underlying the test loses sight of the statutory principle that a director serves only a limited term of office. This principle insures that the shareholders have the right to redetermine corporate policy periodically, if they wish to do so, by electing new directors who favor policy changes. An incumbent board, of course, has authority to implement its policies during its term of office, and this is normally so even though the effects of its action will persist beyond its term. But the board need not use the corporate proxy machinery in connection with the election of directors to achieve such a purpose. When an incumbent board seeks to use the corporate proxy machinery to speak to a policy issue in the context of an


28 See p. 1506 infra.


election campaign, it must necessarily be addressing itself to policy the corporation should follow after expiration of the board's term of office; that is, to policy which the incumbent board has no authority to implement. In this, if the statutory principle of a limited term of office is to be respected, its members must be regarded as acting not as officeholders but as officesekers.

In terms of fiduciary duties also, the rationale underlying the policy-information-reasonability test loses sight of the crucial fact that toward the expiration of his term an incumbent director assumes the capacity of officeseeker as well as officeholder, thereby creating an irreconcilable conflict of interest. As to policy issues in dispute between incumbents and insurgents, the director is not a decisionmaker but a proponent who is vitally self-interested in the acceptance of his proposals. A director cannot be left to determine whether the future good of the shareholders requires spending corporate money to elect him to a new term. How many officeholders can resist the temptation of deeming themselves indispensable, particularly if the alternative includes not only being dispensable but being dispensed with? The incumbent's judgment concerning the effects of policy proposals must be regarded as the platform of a candidate seeking election, rather than the disinterested policy of a fiduciary, simply because in such matters the incumbent himself cannot say honestly in which capacity he acts. Both in terms of authority and strict fiduciary standards, the presence of a policy issue in a proxy fight should not in itself justify board access to the corporate proxy machinery.

Not surprisingly, considering the substantive defects of the rationale underlying the policy-information-reasonability test, it has proven to be incapable of meaningful application. Although the test is based on a distinction between policy and personnel matters, in fact almost everyone, even courts purporting to apply the test, agrees that this distinction is meaningless, that every

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31 This analysis is applicable whether or not the board is a classified one. Although in elections to a classified board the incumbents may not all be officesekers, they are typically all campaigners. The members of such boards normally form a cohesive control group, without regard to the classification, and incumbents must back a winning slate at each election or soon lose control.

32 If a doctrine may be judged by its fruits, it need only be added that the policy rationale has been further applied to reach the grotesque result that a board may legally spend corporate funds to buy out potential insurgents in order to prevent a policy issue from ever coming before the shareholders. See Cheff v. Mathes, 41 Del. Ch. 494, 504, 199 A.2d 548, 554 (1964); Kors v. Carey, 39 Del. Ch. 47, 55, 158 A.2d 136, 141 (1960). But see Bennett v. Propp, 41 Del. Ch. 14, 20–22, 187 A.2d 405, 408–09 (1962). See generally Brudney, supra note 23, at 259–85; Note, Buying Out Insurgent Shareholders with Corporate Funds, 70 YALE L.J. 308 (1960).
contest involves or can be made to involve issues of policy, and that even issues of personnel are often issues of policy. Although the test requires that the expenses be for the purpose of informing shareholders concerning the policy issue, in fact many common proxy contest expenses—such as those for entertainment and public-relations counsel—are better suited to high-pressured efforts at persuasion than to imparting hard information and could not easily be justified on an informational basis. And although it is intrinsic to the test that the expenses be "reasonable," no workable standard has been enunciated by which such reasonability is to be judged. Apart from a New York lower-court decision advertimg to the relationship between the amount involved and the size of the corporate structure, most of the cases do not bother to state criteria of reasonability, and the commentators have supplied either no gloss at all, or gloss so meaningless as a requirement that the expenses be "ordinary and necessary," or that they "bear a substantial relationship to... full information dispersion to the stockholders..." Thus the three-pronged policy-information-reasonability test is really no test at all, and there seems to be only one modern case which has applied it to restrict management's use of the


37 E.g., Comment, Corporate Policy, the "Cure-all" for Proxy Solicitation Ailments?, 49 Mich. L. Rev. 605, 610 (1951) ("The most that can be done in the way of asserting a principle is to take sanctuary behind the time-worn generalization that such expenditures are reasonable if necessary will be upheld." (emphasis in original)); cf. Note, supra note 33, at 236-37.


39 Comment, supra note 33, at 51 (emphasis in original). See also Machtinger, supra note 33, at 214 ("necessary to the informational process").

corporate proxy machinery. Some commentators have reacted by suggesting a flat prohibition against charging the corporation for such common campaign techniques as proxy solicitors, public relations counsel, entertaining, and the like, on the ground that they are not really designed to impart information, and therefore cannot be justified on the basis that the board has authority to inform the shareholders. Yet, while the proposition that corporate payment for these techniques cannot be justified on such a basis is correct, the proposition that it cannot be justified on any basis is not.

In considering this problem two economic facts must be viewed in conjunction: (1) Proxy fights involve a lot of money—a recent estimate is forty thousand to one million dollars—and most of the expenses are probably incurred in connection with just those techniques that have the least informational content; (2) While corporate directorships are unquestionably valuable, in themselves they do not normally pay very much money. A survey of 456 manufacturing corporations showed that outside directorships paid average annual fees of $2800–$3600, while inside directorships paid little or nothing (although some inside directors of course command high salaries and fringe benefits in their executive capacities). Putting these two facts together, most outside directors and many inside directors ordinarily could not be expected to defend a proxy fight out of their own pockets. Thus a rule which precluded management from using corporate resources for such campaigns might tend to drive corporate offices into the hands of those who are ready and able to pay for such campaigns. Management access to the corporate proxy machinery may therefore be justified, not because the election of directors is

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42 See F. Emerson & F. Latcham, supra note 4, at 73 (last minute messages); Friedman, supra note 33, at 954–55 (proxy solicitors); Note, 44 Geo. L.J., supra note 35, at 306–07 (proxy solicitors, public relations counsel, and other "high pressure methods").
44 See pp. 1494–95 supra.
45 See J. Bacon, Corporate Directorship Practices 32–54 (1967). Ninety-seven percent of the reporting manufacturing corporations paid fees to outside directors. See id. at 29–30. The median per-meeting fee of these corporations was $400, and their median number of directors' meetings was seven to nine. Id. at 29, 127 (Table 21B). Many of these corporations, however, pay additional fees for committee meetings. Id. at 31. Three-fourths of the reporting manufacturing corporations did not pay inside directors additional fees for their service. Of those which did, the median per-meeting fee was one hundred dollars. Id. at 56–57.
a board function — it is not; and not because typically the issues are policy issues and the expenses are incurred for the purpose of informing the shareholders on these issues — they are not; but because in the long run the shareholders and the entire economy might suffer if management had to choose between paying for proxy campaigns out of its own pocket or throwing in the towel.

But conversely, since the only sound justification for permitting management to use the corporate proxy machinery is the desirability of neutralizing personal campaign funds as a determinant of corporate office, management should be permitted to use such machinery only to the extent necessary to accomplish that purpose. To put this differently, the permissibility of a corporate expenditure should turn on whether its purpose is to enable management to meet insurgents on equal terms, on the one hand, or to engulf them, on the other. Just as the campaign chest of insurgents should not determine corporate elections, neither should the held-in-trust wealth of the corporation. If the insurgents engage in an advertising campaign, it is reasonable for management to match them, ad for ad, at the corporation's expense. If the challengers employ public relations counsel or proxy solicitors, or if it is reasonably foreseeable that they will, management should be allowed to do so at the corporation's expense. But management should not be allowed to use the corporate proxy machinery to wage a campaign that substantially exceeds that of the insurgents.

It appears likely that business mores already reflect such a rule. Comparative spending figures are readily available for thirteen contests. In ten of these, management spent either

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47 Normally, management access to the corporate proxy machinery should be restricted to defending against and reacting to actual insurgent campaigning; but where such a restriction would be impracticable, management access should be permitted on the basis of the insurgents' reasonably foreseeable activities. For instance, there are only a limited number of proxy soliciting firms, which differ in ability and which may not be employable on short notice. If management were required to wait to retain such a firm until insurgents did so, it might be unable to retain the firm of its choice, or perhaps any firm at all. Management should therefore be allowed to commit corporate funds to retain such a firm, even if the insurgents have not yet done so, if it is reasonably foreseeable that they will.

48 The possibility that there may be more than one group of insurgents raises the question whether, in such a case, management should have such access to the corporate proxy machinery as to match the total amount spent by all insurgents, or only that of the highest-spending group. Since the sole purpose of allowing management access should be to neutralize personal campaign funds as a determinant of corporate office, management access should be limited to matching the expenses of the highest-spending group unless the groups are acting in concert.

49 In response to a senatorial request to ascertain the costs of six of the then more recent proxy battles, the SEC in 1957 reported the following figures:
less or not materially more than did the insurgents. Of the other three cases, in only one were management's expenses radically disproportionate to those of the incumbents. Thus, the rule proposed would be a shift more in theory than in practice.

What about the other side of the coin? Would a matching test result in an undue drain on the corporate treasury by management? A matching test ties management's reimbursable expenses to the amount spent by the insurgents, and insurgent spending is likely to be limited by the fact that under present rules of law insurgents are not entitled to reimbursement of their expenses as a matter of right. Furthermore, the theory behind a matching test is that insurgents should not be enabled to win elections simply because they are able to feed more money into a campaign than management. If that theory is sound it should apply regardless of how much the insurgents spend; indeed, the more insurgents are prepared to spend, the greater may be the need for corporate reimbursement of management expenses.

While a matching test has not explicitly emerged from the

<table>
<thead>
<tr>
<th>Company</th>
<th>Managements' Expenses</th>
<th>Insurgents' Expenses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alaska Juneau Mining Co.</td>
<td>$23,871</td>
<td>$32,795</td>
</tr>
<tr>
<td>Fairbanks, Morse &amp; Co.</td>
<td>50,000</td>
<td>50,000</td>
</tr>
<tr>
<td>Libby, McNeill &amp; Libby</td>
<td>25,000</td>
<td>19,000</td>
</tr>
<tr>
<td>Seiberling Rubber Co.</td>
<td>35,000</td>
<td>35,000</td>
</tr>
<tr>
<td>Thermod Co.</td>
<td>5,000</td>
<td>25,000</td>
</tr>
<tr>
<td>Virginia-Carolina Chemical Co.</td>
<td>125,411</td>
<td>83,019</td>
</tr>
</tbody>
</table>

Hearings on SEC Enforcement Problems Before a Subcomm. of the Senate Comm. on Banking and Currency, 85th Cong., 1st Sess. 115 (1957). Similarly, E. Aranow & H. Ennorn, supra note 6, at 543, report comparative spending figures for seven contested elections as follows:

<table>
<thead>
<tr>
<th>Company</th>
<th>Managements' Expenses</th>
<th>Insurgents' Expenses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fairchild Engine &amp; Airplane Corp.</td>
<td>$133,955</td>
<td>$127,556</td>
</tr>
<tr>
<td>Sparks-Withington Co.</td>
<td>51,165</td>
<td>6,000</td>
</tr>
<tr>
<td>Thompson-Starret Co.</td>
<td>20,110</td>
<td>25,755</td>
</tr>
<tr>
<td>United Cigar-Whelan Stores Corp.</td>
<td>60,759</td>
<td>39,534</td>
</tr>
<tr>
<td>New York Central R.R.</td>
<td>875,000</td>
<td>1,308,733</td>
</tr>
<tr>
<td>New York, New Haven and Hartford R.R.</td>
<td>94,321</td>
<td>94,384</td>
</tr>
<tr>
<td>Republic Corp.</td>
<td>257,000</td>
<td>365,215</td>
</tr>
</tbody>
</table>

The management figures, however, probably do not attribute any amount to the labor of corporate personnel and the use of corporate facilities. Thus in a case growing out of the 1967 MGM proxy contest, it was reported that the insurgents spent $175,000 while management spent $125,000 “exclusive of amounts normally expended for a solicitation for an election of directors and costs represented by salaries and wages of regular employees and officers.” Levin v. Metro-Goldwyn-Mayer, Inc., 264 F. Supp. 797, 802 (S.D.N.Y. 1967). On the other hand, the insurgent figures probably do not attribute any amount to the value of the insurgents' own time.

See p. 1512 & note 94 infra.
cases, it can be viewed simply as an elaboration of the reason-
ability prong of the conventional policy-information-reasonability test, and indeed may have been at least subliminally so contemplate
by the courts. For example, in *Rosenfeld v. Fairchild Engine & Airplane Corp.*,\(^5\) decided by the New York Court of Appeals, it was said in applying this test:

In the event of a proxy contest, if the directors may not freely answer the challenges of outside groups and in good faith defend their actions with respect to corporate policy . . . the corporation may be at the mercy of persons seeking to wrest control for their own purposes, so long as such persons have ample funds to conduct a proxy contest.\(^5\)

**B. Shareholder Access**

Management access to the corporate proxy machinery derives essentially from state law, although it is recognized implicitly by the Proxy Rules.\(^6\) As to shareholder access, the Proxy Rules go further, for rule 14a-8\(^5\) provides explicitly that certain types of shareholder proposals must be included in the corporation's proxy materials if they are made by a holder of voting securities subject to the Proxy Rules.\(^5\) However, the access so provided is severely restricted in a variety of ways. Most important for present purposes, rule 14a-8 explicitly excepts from its coverage elections to office;\(^6\) for reasons that have never been explained.\(^6\) However, in the case of shareholder access, as in the case of management access, the Proxy Rules do not preempt the field of proxy regulation to the exclusion of state law, but merely set minimum conditions of fair disclosure and fair conduct; beyond these minimum conditions questions concerning the allocation of powers between management and shareholders, including questions concerning power over the corporate proxy machinery, must be an-


\(^{53}\) Id. at 173, 128 N.E.2d at 293 (Froessel, J.) (emphasis added).


\(^{56}\) Proxy Rule 14a-7, 17 C.F.R. § 240.14a-7 (1969), provides that under certain circumstances a corporation must either furnish a shareholder with a shareholder list or, at its option, mail out materials for him at his expense. Although this provision can be used to facilitate communication among shareholders, it does not really provide meaningful access to the corporate proxy machinery, since the shareholder must pay the cost of communication. Apart from cost, the machinery provided by rule 14a-7 is frequently unsatisfactory to the shareholder. *See* 2, 5 Loss 890-94, 2851-53 (2d ed. 1961, Supp. 1969).

\(^{57}\) Proxy Rule 14a-8(a), 17 C.F.R. § 240.14a-8(a) (1969).

\(^{58}\) This exclusion was adopted in 1940, when the SEC first formalized the shareholder-proposal rule. The press release announcing adoption of the rule gave
swered by state law. 59 Let us turn then to an examination, under state law, of the questions: (1) whether the shareholders may designate their candidates for directorships in the corporate proxy materials; and (2) whether the shareholders may use corporate funds to pay the expenses of a campaign on their candidates' behalf.

1. Designation of Candidates for Directorships.—Current practice in connection with the election of directors of publicly held corporations reflects the current assumption that the board has virtually exclusive access to the corporate proxy machinery. The board's candidates for directorships (normally, the members of the incumbent board) are listed and described in a corporate proxy statement prepared in connection with the annual shareholders' meeting; and those same candidates are designated in an accompanying corporate proxy card, in the form of a ballot, which the shareholder is asked to sign and return, thus signifying his vote in favor of the board's candidates. Insurgent shareholders, on the other hand, will normally be forced to send out a separate proxy statement and proxy card listing and describing their candidates, under their own names and at their own expense. Thus, current practice favors an incumbent board in two vitally important ways. First, an incumbent board uses corporate facilities to solicit proxies on its own behalf, while insurgents may have to undertake expensive and time-consuming litigation even to obtain a shareholder list, and must then pay out of their own pockets

the expenses of preparing, clearing, printing, and distributing their proxy statement and proxy card. Second, incumbents gain an important psychological advantage in soliciting under the name of "the corporation" rather than under their own names, as insurgents must do.

Is this practice lawful? While this question must be answered under state law, neither statutes nor cases speak directly to the point. However, several important principles of corporate law each lead to the conclusion that the shareholders are entitled to designate candidates for directorships in any proxy card or proxy statement issued by the corporation which lists candidates' names. These principles are: that the exclusive power to elect the board and the right to nominate candidates for directorships rest with the shareholders; that corporate funds and facilities cannot be applied to the personal benefit of corporate officers; and that corporate assets cannot be applied to the benefit of individual shareholders except in an evenhanded manner.

(a) The Exclusive Power to Elect and the Right to Nominate Rest With the Shareholders. — Under the corporate statutes the power to elect the board is vested exclusively in the shareholders. The board does not have the power to elect its successor board (although it is often empowered to fill interim vacancies caused by death, resignation, or removal), and cannot be given this power without violating the statutes. But to give any group exclusive access to the corporate proxy materials for the purpose of designating its directorial candidates would be virtually tantamount to giving that group the power to elect the board. A rule which conferred such exclusive access on the board itself would therefore conflict with the statutory provisions vesting in the shareholders exclusive power to elect the board. "No one would

60 The issue of management's right to solicit proxies was raised but not decided in Empire S. Gas Co. v. Gray, 29 Del. Ch. 95, 110, 46 A.2d 741, 748 (1946).
61 See note 24 supra.

In Gallagher a bylaw limited corporate office to persons nominated by (a) a committee consisting of the corporate solicitor and two persons appointed by the president, or (b) twenty-five percent of the shareholders. The court in striking down the bylaw stated:
argue that an elected public official should be permitted to extend his own term of office. The same reasoning applies to a corporate director who is also an elected official and a servant of the corporate electorate. 65

As a corollary to their exclusive right to elect the board, the shareholders have the right to nominate candidates for directorships. 66 It has already been shown that the proxy system is today's shareholders' meeting. 67 Correspondingly, the designation of candidates in the proxy materials is today's nomination. The shareholders' right to make nominations should therefore carry with it access to the proxy materials for that purpose. As the only corporate organ with an indisputable legal right to nominate directors, the shareholders cannot be denied legal access to the basic corporate machinery used to make nominations. Although it might be objected that nominations are not made in the proxy materials, but rather from the floor at the annual meeting, such an objection at best is built purely on form, and at worst ignores both current understanding and practice with regard to nominations. Normally, proxies are executed and mailed by shareholders before the date of the meeting, and proxies gathered in a solicitation subject to the Proxy Rules can be voted only in favor of persons named in the proxy. 68 Therefore, if nominations are not deemed to occur until the meeting, voting would precede nomina-

The committee of three has the powers of 25 per cent. of the whole number of stockholders in the matter of nominations. If this committee were freely selected by the stockholders from among themselves, something might be said to vindicate it as a mode of regulating elections. Even then there would be grave objections to be considered. When, however, the solicitor, an officer whose position is peculiarly advantageous, is made one of the three, and the president, who is the highest functionary, appoints the other two, the liability of the scheme to degenerate into a device for the easy re-election of the incumbents is obvious. This committee of three, brought together by the president, acts easily and smoothly. The stockholders themselves are, however, balked at every step. They must form a kind of sub-association or caucus in order to enable them to exercise their individual rights. If they do not, they will find it impracticable to get each one of 25 per cent. of the stockholders spontaneously and at the same instant to hit upon a list of nominees which will prove to be identical with the lists thought out by the other members of the 25 per cent. club. The conclusion seems obvious that the scheme automatically deprives the stockholders of all practical control of the election.

7 Pa. Dist. at 785–86. Other cases have upheld such bylaws where the minimum number of shareholders required to nominate a candidate was more reasonable. See cases cited in note 78 infra.


67 See p. 1494 supra.

68 Proxy Rule 14a-4(d), (e), 17 C.F.R. § 240.14a-4(d), (e) (1969).
tions—a rather unusual format. Indeed, it appears that in actual corporate practice the bylaws usually do not fix the time for making nominations, and that the predominant practice is in fact to treat the proxy materials as nominating machinery, so that persons in whose names proxies are solicited are normally characterized in the proxy materials as "nominees" rather than merely as "candidates." 70

In light of the principle that the shareholders have the exclusive right to elect the board, it might be questioned on what principle the board may use the corporate proxy machinery to designate candidates at all. Such use might be justified on two bases: a customary right of the board to nominate candidates, 71 or application of the principle that as far as reasonably practicable personal campaign funds should not be permitted to determine corporate office. 72 But neither basis would justify exclusive board access to the corporate proxy machinery for this purpose. Even assuming the board has a customary right to nominate candidates, it could not abrogate the shareholders' nomination right, which inheres in the shareholders by law. And if personal campaign funds should not be permitted to determine corporate office, far less should the funds of the corporation itself, as would tend to be the case if the board's access were exclusive.

(b) Corporate Funds and Facilities Cannot Be Applied to the Personal Benefit of Directors.—Corporate funds and facilities cannot be applied to the personal benefit of directors, except for a clearly defined corporate purpose, such as compensation for services. But since a corporate directorship is a position of val-


72 See pp. 1491–1501 supra.
to permit incumbent directors exclusive access to the corporate proxy machinery to designate themselves as candidates would permit them to apply corporate assets to their own personal benefit for no established corporate purpose — indeed, in violation of the corporate principle that power to nominate and elect resides in the shareholders. A corporate ballot prepared for use at the annual meeting could not validly exclude anyone properly nominated for office, nor could it give favored treatment to one group of nominees. The proxy card and proxy statement, when paid for by corporate funds, become the corporate ballot, and should likewise be open to all persons whose candidacies are properly advanced.

Of course, permitting incumbent directors to designate themselves as candidates for office in the corporate proxy materials even on a nonexclusive basis might be characterized as permitting them to apply corporate funds and facilities to their own personal benefit. However, a nonexclusive right is not only significantly less valuable than an exclusive one, but also serves a corporate purpose, since it tends to maximize the number of potential candidates for office and neutralize personal campaign funds as a determinant of office.

(c) Corporate Assets Cannot Be Applied to the Benefit of Individual Shareholders in a Nonevenhanded Manner. — Just as corporate funds and facilities cannot be applied to the personal benefit of directors except for a clearly defined corporate purpose, neither can corporate funds and facilities be applied to the benefit of individual shareholders except in an evenhanded manner. Yet it seems likely that in the majority of corporations in which proxies are solicited management originally achieved office because it held or represented a significant amount of stock. To give "management" the right to designate candidates in the corporate proxy materials while refusing that right to "shareholders" would, in substance, often be to discriminate among shareholders on the basis of whether they were in or out at the time of the solicitation.

That corporate assets cannot be applied to the benefit of

72 See pp. 1494-95 supra.
74 A grant of exclusive access could not be justified on the ground that it constituted compensation of the directors, because the "compensation" would in effect consist of a term longer than that legally provided for. Cf. State ex rel. Ryan v. Cronan, 23 Nev. 437, 452-53, 49 P. 41, 45 (1897).
76 Cf. Eisenberg, supra note 2, at 33-48.
shareholders in a nonevenhanded manner does not mean that each individual shareholder must have the right to designate candidates for directors in the corporate proxy materials. No sound reason appears why a bylaw, at least a shareholder-adopted bylaw, could not limit such access, provided that it did so in an evenhanded and reasonable way. Thus bylaws could validly provide that candidates for director may be designated in the corporate proxy materials only by the board (or some committee thereof) and by shareholders holding in the aggregate some minimum percentage of the corporation's outstanding stock—say five percent. The courts have upheld comparable bylaws restricting the shareholders' right to nominate candidates for corporate office, upon which the right to designate candidates in the corporate proxy materials is partially based.

The conclusion drawn so far is a very limited one: The shareholders as a body have the right to designate candidates for office in the corporate proxy materials, but this right may be circumscribed by reasonable bylaws. It does not necessarily follow that shareholders can use the corporate proxy machinery to pay the expenses of a proxy campaign, a question which will be discussed below. Nor does it follow that management is prohibited from grouping its candidates together and designating these can-


79 See pp. 1511–17 infra.
didates as the management slate—a slate that would probably be elected in the normal course of things. I recognize, however, that this conclusion will nevertheless strike many as unconventional—unconventional perhaps to a fault. Let me therefore attempt to anticipate three kinds of argument that might be made against it.

One argument, which stems from the conclusion's apparent unconventionality, is that even if shareholders might once have claimed the right to designate candidates in the corporate proxy materials, a contrary practice of denying that right has grown up which it is now too late to challenge. In fact, however, it seems highly unlikely that such a practice could be proved, if only because the assertion of the right is so seldom made. True, management has probably assumed that shareholders do not have access to the corporate proxy machinery except under rule 14a-8, and others, including shareholders, have probably assumed either that management's assumption was correct or that in any event management would deny shareholders' requests for such access. But an assumption hardly constitutes a practice, particularly when the assumption has for most purposes not been relied upon by those who might set it up as a defense. Furthermore, this assumption has not been universally accepted, and where accepted it has been accepted uncritically. Finally, even if a practice of denying access to shareholders could be proved, it should not be enshrined as a rule of law, given its self-serving nature, its conflict with significant principles of corporate law, and its own lack of principled justification.

A second possible argument against the right of shareholders to designate candidates in the corporate proxy materials is that such a result would be impracticable. Obviously, practicability should be considered in determining the rules governing access to the corporate proxy machinery. It does not seem impracticable, however, to permit the shareholders to designate candidates through that machinery. Such access need be triggered only when the corporate proxy machinery is set in motion for a similar purpose by management. Such access need be triggered only when the corporate proxy machinery is set in motion for a similar purpose by management, and therefore would not entail the distribu-

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80 Such a conclusion is not, however, entirely unprecedented. Cf. Brudney, supra note 23, at 284; Caplin, Shareholder Nominations of Directors: A Program for Fair Corporate Suffrage, 39 Va. L. Rev. 141, 151-54, 159-61 (1953); Friedman, supra note 33, at 959 n.31; Stifel, supra note 11, at 348; Note, supra note 11, at 1168 n.23.


82 See note 80 supra.

83 See the remarks of Lord Denman quoted at p. 1489 supra. See also C. Allen, Law in the Making 329-34 (7th ed. 1964).
tion of corporate proxy materials that would not otherwise be distributed; all that would be required is the addition of extra names to a proxy card and extra names and descriptions to a proxy statement being distributed anyway. Furthermore, since the corporate proxy machinery will predictably be set in motion at approximately the same date every year, a shareholder's exercise of this right could be conditioned on the submission of the names of his candidates a reasonable time in advance of this date. Thus where the right is exercised — and it will not always be exercised — it is doubtful that it would add materially to the basic solicitation cost. And corporations which deem an unrestricted shareholder right to designate candidates impracticable can adopt a bylaw limiting the right to shareholders owning in the aggregate some minimum percentage of the corporation's stock, say five percent. If it is practicable to spend corporate funds to designate management candidates for office, it is not impracticable to spend some small additional funds to designate the candidates of a shareholder group owning such a percentage of the corporation's stock.

A third possible argument is that as a matter of policy it is preferable to maximize managerial power and minimize the power of shareholders. Such an argument is normally made to rest on one of two different premises: (1) That management knows better than the shareholders themselves what is good for the shareholders, so that the shareholders' own best interests are promoted by limiting shareholders' rights; or (2) That the public interest is best advanced by scaling down the shareholders' interests in favor of corporate client-groups, such as labor or consumers, and that to accomplish this purpose it is necessary to weaken shareholder control over management, which is then in a position to recognize client-group claims. Both premises seem defective at this point in time.

The first premise assumes that the average shareholder is economically naive. However, as I have pointed out in an earlier article, while the average shareholder may be economically naive (although even this has not been proved), the vast bulk of shareholdings are apparently controlled by sophisticated and wealthy individual or institutional investors who are very well able to calculate their own interests. The second premise assumes

87 Eisenberg, supra note 2, at 33-48.
that ultimate shareholder control prevents management from being responsive to the due interests of others. In fact, however, even if ultimate shareholder control reinforces a corporate orientation toward profit maximization, it does not prevent management from behaving decently. In the long run, the public interest might better be served by a corporate orientation toward maximizing profits within the limits of decent behavior than by dropping profit maximization as the principal corporate goal. But, in any event, there is no sound basis for believing that ultimate shareholder control does significantly affect corporate orientation toward profits, or that present-day management could or would use a less circumscribed power either wisely or selflessly. Managers, no less than shareholders, are deeply self-interested in many of the most important corporate decisions, and generally speaking there is nothing in the present education of managers, or the present process of managerial selection, to make one believe that managers are experts on questions of public interest. This is not to argue that shareholders are necessarily more apt to vote in the public interest than are directors; the question is presently indeterminable. Yet, since the shareholders' right to designate candidates follows from general corporate principles, the policy argument against the right is really an argument against implementation of those principles—most particularly the statutory principle that shareholders have the right to elect directors. Since this is a statutory principle, it is questionable whether a policy argument based on the principle's unwisdom could be appropriately addressed to the courts at all; certainly, however, it should not be accepted when it is based on nothing but an unproved if not unprovable premise.

2. Payment of Campaign Expenses. — Assuming that shareholders have the right to designate candidates in the corporate proxy materials, do they also have the right to use corporate funds to wage a campaign on their candidates' behalf? Preliminarily, it should be observed that under the rules delineated so far, this question may have a more limited significance than is usually


90 See Eisenberg, supra note 2, at 27-30.

assumed. If the shareholders have access to the corporate proxy machinery to designate their candidates for directorships, and if the board may spend corporate funds for a campaign only to match insurgent campaign spending, management’s access to the corporate treasury to pay for a proxy campaign would not become operative if the insurgents limited their attack to the designation of their own candidates in the corporate proxy materials. Admittedly, however, given the momentum of power, most insurgents probably would be unwilling to run a proxy fight on such a modest basis; and if they do campaign, we have seen that management would have a right to use corporate funds and facilities for a counter-campaign. Strict application of the principles applicable to designation of directorial candidates in the corporate proxy materials might then seem to require that the insurgent shareholders should have a comparable right to be reimbursed for their campaign expenses. Furthermore, a proxy fight, even if unsuccessful, may produce discernible corporate benefits, such as providing shareholders with an opportunity to choose between competing philosophies and personnel, keeping management generally responsive to shareholders, and exposing management shortcomings which would not otherwise come to light and management policies which may be improved by close scrutiny. Yet the little authority in point indicates that insurgents, unlike management, are not entitled to reimbursement of campaign expenses as a matter of right. Is this authority sound?

Unlike a shareholder right to designate candidates in the cor-

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92 Cf. Steinberg v. Adams, 90 F. Supp. 604, 608 (S.D.N.Y. 1950); F. Emerson & F. Latcham, supra note 4, at 75-79; Brudney, supra note 23, at 284; Friedman, supra note 33, at 926.

A distinction is sometimes drawn between management and insurgents on the ground that management has a duty to fight off insurgents advocating a policy which management believes ill-advised, while insurgents have no duty to begin a proxy fight. See, e.g., Note, supra note 35, at 309-10. This argument is essentially a variant of the policy rationale for board access, discussed at pp. 1496-99 supra. Perhaps incumbents are under a duty to call to the shareholders’ attention misrepresentations by persons seeking corporate office; but they are under no duty either to stand for reelection, or to challenge merely problematical assertions concerning business policy made by opposing candidates.


porate proxy materials, the right to reimbursement of campaign expenses would raise severe prudential problems. A right to full reimbursement of expenses might cause substantial drains on the corporate treasury, for many shareholders would undoubtedly regard such a right as an invitation to wage proxy fights annually at the corporation's expense. But the establishment of a principle by which to delimit insurgent reimbursement is no easy task. A defensive matching concept, such as that applied to management, would obviously be inappropriate for application to insurgents. Theoretically, perhaps, reimbursement might be limited to the benefit resulting from the insurgents' campaign; but, since such benefits are normally intangible and unquantifiable by a judge or jury, this could not be applied in practice. As a fallback, reimbursement might be limited to that portion of the insurgents' expenses attributable to an informational function. That determination would be very difficult to make, however, and even such a limited right could easily drain the corporate treasury when there was more than one insurgent group, as would often be the case if such a rule were adopted.

Commentators favoring insurgent reimbursement have proposed various implementing formulas which seem to be constructed with at least one eye on the prudential problem. Under one formula, for example, insurgents would be reimbursed if, but only if, they achieved some minimum amount of voting support, say ten or fifteen percent. Under another, each insurgent group would be reimbursed an amount bearing the same relation to the number of votes achieved by its slate as management reimbursement bears to management votes. Under still a third, each group would be reimbursed a percentage of its expenses which depended on its percentage of total votes — for example, full reimbursement if it gathered fifty percent of total votes, ten percent reimbursement if it gathered five percent of total votes.

Generally speaking, these formulas do not fully solve the multi-insurgent problem. Permitting reimbursement of any insurgent group which gathered ten percent of the votes could result in cases where several groups might so qualify. Limiting reimbursement to an amount based on the ratio between management

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95 See Comment, supra note 93, at 686; 43 Calif. L. Rev. 893, 903 n.53 (1955).
96 Cf. 43 Calif. L. Rev. 893, 903 (1955); 36 Cornell L.Q. 558, 563-64 (1951).
98 See Stifel, supra note 11, at 347.
99 See, e.g., F. Emerson & F. Latcham, supra note 4, at 76-78; Emerson & Latcham, Proxy Contests: A Study in Shareholder Sovereignty, 41 Calif. L. Rev. 393, 435 (1953); Friedman, supra note 33, at 563.
100 Emerson & Latcham, supra note 99, at 435-36.
101 See Comment, supra note 93, at 691-92.
reimbursement and management votes would provide no effective ceiling where the management vote was very low. Even the third test, although a considerable improvement in this respect over the first two, could result in reimbursement of substantially all the expenses of two insurgent groups where management received a very low vote.

But there is another, very different kind of objection to all three formulas. While legislative adoption of one of these formulas, or some analog, might seem desirable, none seems appropriate for judicial adoption, since all find expression in mathematical formulas rather than in principled terms. And this difficulty seems indigenous to the problem rather than unique to these particular tests.

There is, however, a more modest solution of the problem which is within the judicial competence, and which has in fact been adopted by courts. In Steinberg v. Adams and Rosenfeld v. Fairchild Engine & Airplane Corp., it was held that although insurgents may not be entitled to reimbursement of their expenses as a matter of right, a corporation has the power to reimburse such expenses. This rule tends to equalize management and shareholder access to the corporate proxy machinery, yet satisfies, without resort to formulas, the prudential considerations discussed above. The rule would seldom, if ever, result in reimbursement of more than one insurgent group, because as a practical matter the corporation will seldom exercise such a power except in favor of successful insurgents. Of course, even reimbursement of one insurgent group may cause an undue drain on the corporate treasury. In most cases, however, undue spending would not be encouraged by the rule itself; since reimbursement under the rule is not a matter of right, insurgents must initially

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106 In some cases insurgents may be reimbursed where they are only partially successful. Cf., e.g., Reading to Ask Holders to Approve Payments of $79,000 to Dissidents, The Wall St. J., May 19, 1966, at 8, col. 1. But it is unlikely even in these cases that more than one group would be so reimbursed.
risk their own money. This risk should serve to check their spending.

Yet suppose a case in which the insurgents regard the possibility of losing the election as minimal. This normally could occur only where the insurgent group holds a substantial amount of stock. High campaign spending will be counterproductive for such insurgents, since it will drain cash out of the corporate treasury — not only the cash the insurgents spend, but that spent by management. Insurgents who regard the possibility of loss as minimal should tend to underspend rather than overspend.

A more likely case for unduly high insurgent spending would occur where the insurgents are unsure of victory, but the rewards of victory would be very great. Even in this case, since the prize may not be won (and if won may be decreased in value by the very campaign to achieve it), the insurgents' self-interest should normally serve as a check on their spending. Nevertheless, many would probably feel that a check other than the insurgents' own self-interest is necessary, and support for such a position can be drawn from Rosenfeld and Steinberg, both of which indicate that only the insurgents' "reasonable" expenses may be reimbursed. But how is reasonability to be measured in this context? One possibility would be to limit reimbursement to those expenses which are attributable to an informational function. This would give maximum protection to the corporate treasury: directly, in limiting permissible reimbursement of insurgent expenses, and indirectly, in tending to hold down insurgent spending and therefore reimbursable management spending. Such a test would, however, be very difficult to administer. Furthermore, since insurgents will frequently spend money on noninformational functions even if such spending cannot be reimbursed, while management's matching expenses normally would be reimbursable, such a test would maintain a substantial disparity between the access of management and shareholders to the corporate proxy machinery. It therefore seems preferable to adopt a limitation which

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107 If the solicitation comes under the Proxy Rules, the insurgents are also subject to the check of prospective disclosure, since they must state in their proxy statement "the total amount estimated to be spent and the total expenditures to date for, in furtherance of, or in connection with the solicitation of security holders" and "whether reimbursement will be sought from the issuer . . . ." Proxy Rules 14a-3(a), Schedule 14A, Items 3(b)(4), (5), 17 C.F.R. §§ 240.14a-3(a), 240.14a-101(3)(b)(4), (5) (1969).


depends not on the nature of the expense, but on the gross amount spent—for example, by limiting reimbursement to the average amount spent in proxy fights of corporations of similar size in terms of assets, and number and distribution of shareholdings.¹¹⁰

A final question: which corporate organ must approve reimbursement? The case law seems to assume that the board has power to reimburse management's proxy fight expenses.¹¹¹ This seems to square with the underlying substantive rule, since if management has a right to reimbursement, payment merely constitutes the discharge of a rightful claim, and therefore falls within the board's power to manage the corporation's business. Indeed, if management reimbursement required shareholder approval it would not be a right at all, since shareholder approval might not be forthcoming if the insurgents win.

Some commentators have argued that the board should also have power to reimburse insurgents,¹¹² apparently on the theory that the treatment of management and shareholders should be equalized as far as possible. But the exercise of a discretionary power to reimburse persons for expenses incurred in gaining control of the corporation does not seem to constitute management of the corporation's business in any ordinary sense of that term.¹¹³ Both Rosenfeld¹¹⁴ and Steinberg¹¹⁵ indicate that the reimburse-

¹¹⁰ Some figures on the cost of past fights have already been published. See note 50 supra. Other figures are available from proxy statements on file with the SEC. See note 107 supra.

¹¹¹ See Hand v. Missouri-Kansas Pipe Line Co., 54 F. Supp. 649 (D. Del. 1944); Hall v. Trans-Lux Daylight Picture Screen Corp., 20 Del. Ch. 78, 171 A. 266 (1934); Streett v. Laclede-Christy Co., 409 S.W.2d 691, 698-99 (Mo. 1966). In each of these cases shareholder approval had not occurred, nor was it in prospect, but the court nevertheless held that management access to the corporate proxy machinery was proper if the policy-information-reasonability test could be met. In Rosenfeld v. Fairchild Engine & Airplane Corp., 309 N.Y. 168, 173, 128 N.E.2d 297, 293 (1955), shareholder approval had occurred, but the language of Judge Froessel's opinion indicated fairly clearly that he did not regard such approval as a necessary condition to management access:

The rule then which we adopt is simply this: In a contest over policy, as compared to a purely personal power contest, corporate directors have the right to make reasonable and proper expenditures, subject to the scrutiny of the courts when duly challenged, from the corporate treasury for the purpose of persuading the stockholders of the correctness of their position and soliciting their support for policies which the directors believe, in all good faith, are in the best interests of the corporation. The stockholders, moreover, have the right to reimburse successful contestants for the reasonable and bona fide expenses incurred by them in any such policy contest, subject to like court scrutiny. (Emphasis added.)

¹¹² See Machtinger, supra note 33, at 217; Note, supra note 33, at 234-35; 24 U. Cinn. L. Rev. 606, 609 (1955).

¹¹³ See Eisenberg, supra note 2, at 11-12, 86-91.


¹¹⁵ 90 F. Supp. 604, 607-08 (S.D.N.Y. 1950). Later in the opinion Judge Rifkind indicated that he might require board as well as shareholder approval:
ment of insurgents requires shareholder approval, and this seems proper if insurgent reimbursement is regarded as a corporate power rather than as a matter of right.

II. Access to the Corporate Proxy Machinery in Connection With Matters Other Than Election to Office

A. Management Access

Management access to the corporate proxy machinery in connection with matters other than election to office is not as difficult to rationalize as its access in connection with election matters. In soliciting votes on a nonelection matter, the board frequently acts within its explicit statutory authority, since the statutes provide that many matters which require shareholder approval must be initiated by the board and then submitted by the board to the shareholders. Even where the statute does not explicitly so provide, most recommendations to shareholders on nonelection matters would probably fall within the board's residual power to manage the corporation's business. Furthermore, since most actions requiring shareholder approval must be approved by a percentage of shares outstanding, rather than merely a percentage of shares actually voting, the lack of a solicitation might often result in a failure to consummate advantageous corporate actions. Similarly, in terms of fiduciary concepts, nonelection

"It seems permissible to me that those who advocate a contrary policy and succeed in securing approval from the stockholders should be able to receive reimbursement, at least where there is approval by both the board of directors and a majority of the stockholders." Id. at 608. See also Grodetsky v. McCrory Corp., 49 Misc. 2d 322, 323-24, 267 N.Y.S.2d 356, aff'd mem., 27 App. Div. 2d 646, 276 N.Y.S. 2d 842 (1966), motions for leave to appeal denied, 29 N.Y.2d 582, 226 N.E.2d 708, 20 N.Y.2d 644, 230 N.E.2d 740 (1967).

Eisenberg, supra note 2, at 61-68.

In contrast, usually only a plurality of the votes cast, or a majority of the votes cast or present, is required to elect directors, provided a quorum is present. See generally ABA Model Bus. Corp. Act § 30, at 480-95 (1960); Caplin, Proxies, Annual Meetings and Corporate Democracy: The Lawyer's Role, 37 Va. L. Rev. 653, 689 n.82 (1951). Quorum requirements for regular shareholder meetings vary among publicly held corporations, but few if any would require more than a majority of outstanding shares, and many probably require substantially less. See, e.g., By-Laws of American Express Co. § 2.4 (majority); By-Laws of American Machine & Foundry Co., Apr. 1, 1969, art. I, § 5 (majority); By-Laws of Anaconda Co., as amended to Feb. 27, 1967, art. 2, § 5 (one-third); By-Laws of Avco Corp., as amended through Apr. 25, 1969, art. II, § 3 (majority); By-Laws of Eastman Kodak Co., as amended through Feb. 20, 1969, art. I, § 5 (majority); By-Laws of General Motors Corp. § 11 (thirty percent); By-Laws of Mobil Oil Corp., as amended to Sept. 27, 1963, art. II, § 4 (one-third).
matters do not involve an inherent conflict of interest, as election matters do. Normally, then, in nonelection matters the board should be able to prepare and mail a notice of meeting, proxy card, and proxy statement describing the proposed transaction, at corporate expense; 110 and since the affirmative vote of at least a majority of outstanding shares must ordinarily be obtained, the board should also normally be able to utilize the corporate proxy machinery for follow-up techniques such as mailings and phone calls to shareholders, advertisements, and the use of professional proxy solicitors. 120

But what if the matter is one in which the board is interested? If the usual legal rules governing self-interested transactions were applicable to the board’s use of the corporate proxy machinery in such cases, 121 the burden might be on the board to defend that use. In the long run, therefore, such treatment might work against the interest of shareholders as a class by discouraging management from submitting proposals to shareholders. Furthermore, the usual self-interested transaction is fully consummated by management, while in cases involving access to the corporate proxy machinery, final action is by hypothesis in the shareholders’ hands.

A distinction might be drawn, however, between cases where a matter being submitted to the shareholders carries a benefit to management in its train, and cases in which a matter consists solely of such a benefit. An example of the former would be a merger involving retention of members of the board as officers and directors of the reconstituted corporation; examples of the latter would be a recommendation that the shareholders ratify a questionable board action, or a proposed certificate amendment increasing directors’ indemnification rights. Even in the latter type of cases it might be inappropriate to apply the usual rule governing self-interested transactions to the expense of distributing the normal corporate proxy materials required to present the proposal fairly — specifically, the proxy statement and proxy card. But if in such a case the board goes further, and engages in a solicitation campaign at corporate expense, perhaps the usual self-interest rules should be applicable to that expense.


120 See Rosenfeld v. Fairchild Engine & Airplane Co., 309 N.Y. 168, 172-73, 128 N.E.2d 191 (1955) (Froessel, J.); E. Aranow & H. Einhorn, supra note 6, at 558; Friedman, supra note 33, at 953-54.

121 By “the usual rules” I mean those rules applicable to a classical self-dealing transaction; the precise content of such rules varies from state to state. See W. Cary, supra note 1, at 557-59, 565-66; 1 G. Hornstein, supra note 1, § 439; Marsh, supra note 46, at 36-48.
At the least, the self-interested nature of the transaction should render inoperative the business judgment rule, so that the board may be held responsible for any such expense which a shareholder can show would probably not have been incurred by a wholly disinterested fiduciary. 122

B. Shareholder Access

i. Shareholder Initiated Proposals.— (a) Right to Access.— Proxy Rule 14a–8 gives the shareholders access to the corporate proxy materials in order to submit certain proposals on matters other than election of office. However, the access so provided is restricted in important ways. For one thing, the Proxy Rules are not applicable to all corporations which solicit proxies. 123 For another, rule 14a–8 does not cover all shareholder proposals which are proper subjects for shareholder action under state law. Management may refuse, for example, to include a proposal without violating rule 14a–8, even though the proposal is a proper subject for shareholder action under state law, if it “consists of a recommendation or request that the management take action with respect to a matter relating to the conduct of the ordinary business operations” 124 or “[i]f it clearly appears that the proposal is submitted by the security holder . . . primarily for the purpose of promoting general . . . social . . . causes.” 125

122 If the shareholders approve the substantive proposal, arguably the approval might also be deemed a ratification of the manner in which the board used the corporate proxy machinery to obtain it. The effect, however, of shareholder ratification in general is unclear. See x G. HORNSTEIN, supra note 1, at 457-59, 543, 557; Comment, Shareholder Validation of Directors’ Frauds: The Non-Ratification Rule v. The Business Judgment Rule, 58 NW. U.L. REV. 807 (1964). And it is questionable whether shareholder approval of a substantive matter should be deemed ratification of the techniques by which approval was obtained when that question is not directly voted upon. Certainly approval should not be deemed to be such a ratification where the shareholders are not given information concerning those techniques and their costs.


A proposal may also be omitted under rule 14a–8 “if the management has at the security holder’s request included a proposal in its proxy statement [during the previous two years] and such security holder has failed without good cause to present the proposal, in person or by proxy, for action at the meeting,” Proxy
light of these limitations on the ambit of rule 14a–8, the question arises whether state law gives shareholders access to the corporate proxy materials for the purpose of submitting proposals on nonelection matters.

If it is lawful for the board to use the corporate proxy materials to submit proposals to shareholders which are within the board's authority to initiate, it should follow that it is lawful for shareholders to use these materials to submit proposals which are within the shareholders' authority to initiate—at least in a corporation in which there is a custom of submitting proposals to shareholders through the proxy materials. To take a case in which the propriety of shareholder access is relatively clear, under some corporate statutes voluntary dissolution is completely within the shareholders' power—the board is given no statutory role either in initiating or consummating the transaction. Suppose that the shareholders of a corporation governed by such a statute wish to have it dissolved. Surely if the proxy materials had been used in the past to present proposals to shareholders

Rule 14a–8(c)(3), 17 C.F.R. § 240.14a–8(c)(3) (1969), or has been submitted to the shareholders within the previous five years and has failed to receive a specified percentage of the total votes cast, the exact percentage depending on the number of times the proposal was submitted during the relevant period. Proxy Rule 14a–8(c)(4), 17 C.F.R. § 240.14a–8(c)(4) (1969). Even where a proposal must be included under rule 14a–8, if management is opposed, the shareholder's supporting statement is limited to one hundred words. Proxy Rule 14a–8(b), 17 C.F.R. § 240.14a–8(b) (1969).

Recent events serve to underline the significance of the ordinary-business-operations and promotion-of-social-cause exclusions. Earlier this year, Ralph Nader announced the formation of the Project on Corporate Responsibility, whose objective is to reform corporate policies, most immediately General Motors' policies, through use of the corporate proxy machinery. Among the proposals the Project desired to submit for consideration by GM's shareholders at this year's annual meeting were that GM improve the design of its cars so that occupants wearing proper seat and shoulder belts can survive, without injury, crashes at sixty miles an hour; that GM cars comply, as promptly as possible, with proposed standards of vehicle emissions recommended by the National Air Pollution Control Administration, but not now mandatory; and that a shareholder committee for corporate responsibility be established, which would have full access to GM's files and employees, and would report to the shareholders at a future annual meeting. Nader To Press for G.M. Reform, N.Y. Times, Feb. 8, 1970, at 44, col. 1; G.M. Urged to Respond to Corporate Need, N.Y. Times, Feb. 22, 1970, § 1, at 49, col. 1. GM management refused to include these proposals in the corporate proxy materials—probably on the ground that they fall within one or both of these exclusions. See Nader Panel Rebuffed by G.M. on Plea to List Consumers' Demands, The Wall St. J., Mar. 6, 1970, at 14, col. 2. The SEC ruled, however, that the resolution to establish the shareholder committee (and a resolution to increase the size of the board) must be included in the GM proxy statement. See G.M. Told to Put Consumer Moves to Stockholders, N.Y. Times, Mar. 20, 1970, at 1, col. 5 (city ed.).

they could be used for a dissolution proposal; and surely, too, the corporate organ with the right to use the materials for this purpose would be the organ with exclusive statutory power to initiate and consummate voluntary dissolution, that is, the shareholders.

But suppose a case in which the question is not so clear. In *Carter v. Portland General Electric Company*, 127 several shareholders of a corporation which was not subject to the Proxy Rules, but which solicited proxies, requested that a statement opposing management’s plans to construct a dam be included in the proxy materials for a forthcoming annual meeting. Management refused. When one of the shareholders attempted to present a resolution opposing the dam from the floor at the annual meeting, the chairman ruled him out of order. An action was then brought to compel management to submit the statement to the shareholders, and to restrain management from making any proxy solicitation which did not include the statement. The plaintiff’s primary theory was that the court should “judicially adopt rules promulgated by the Securities Exchange Commission in respect to proxy solicitation.” 128 This the court refused to do:

Here, if we adopt the rule it would be without limitation. It would apply to any stockholder of any corporation. Nor does there exist any administrative body to make any preliminary determination that a stockholder’s proposal is a “proper” one. In simple reality we would be acting in a void. We do not nor is there any means by which we could know the ultimate repercussions of such a rule. We know that it could be invoked for harassing purposes that could only be avoided by extensive litigation. We must be aware that to judicially impose the suggested rules in these circumstances might well impair rather than benefit the orderly development of this important area of the law of corporations.

Secondly, we do not think that the proposal in this case was one that was necessarily proper for the stockholders to give an advisory opinion about . . . 129

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128 Id. at 403, 362 P.2d at 767.
129 Id. at 406-07, 362 P.2d at 769.

In *Dyer v. SEC*, 289 F.2d 242 (8th Cir. 1961) and *Dyer v. SEC*, 266 F.2d 33, 41-44 (8th Cir. 1959), Dyer, a shareholder in Union Gas, sought review of SEC orders permitting Union Gas proxy materials to become effective, on the ground, *inter alia*, that the materials did not include various proposals made by Dyer pursuant to rule 14a-8. The Eighth Circuit held that rule 14a-8 did not require inclusion of the proposals in question. In the course of its opinions it stated that the rule “affords a privilege, which does not otherwise ordinarily exist in favor of stockholders,” 266 F.2d at 41, and is “not an inherent stock-ownership right,”
Plaintiff’s counsel certainly did not present his best case by placing primary emphasis on the assertion that Oregon should judicially adopt the SEC’s Proxy Rules. Understandably, a state court would be leery of embracing a detailed regulatory scheme which was authorized by Congress, conceived with the assistance of long administrative experience, and intended to apply on a national level only to certain corporations. This flaw in plaintiff’s posture is reflected in the theme running through the court’s opinion that it would be inappropriate to adopt the Proxy Rules without “a comprehensive study of the facts,” preferably a “legislatively created stud[y] . . . .” To the extent that the case turned on this theme, rather than on consideration of state law principles, its precedential value on the state law issue is questionable. Furthermore, that portion of the opinion relating to a shareholder’s right to require inclusion of proposals concerning a proper subject for shareholder action seems to be have been infected by the court’s determination that the proposal at issue was not a proper one. Although couched in terms of an alternative holding, it is not clear that the case would have gone the same way if the court had viewed the particular proposal as proper.

But insofar as Carter does hold that under state law a shareholder has no access to the corporate proxy machinery to make proposals which are proper subjects for shareholder initiation, it is unpersuasive. The court placed some weight on the argument that there is no “administrative body to make any preliminary determination that a stockholder’s proposal is a ‘proper’ one.” If this is really relevant, it would follow that when management refuses to accede to a shareholder request to present a proposal from the floor at the annual meeting, or to call a special shareholders’ meeting, it can foreclose judicial cognizance of the ensuing shareholder claim simply by resting its refusal on the talismanic ground that the proposal does not concern a proper subject for shareholder action. Too bad for shareholders in Oregon

289 F.2d at 245. These statements must be evaluated in the context in which they were made. The issue was not what state law required, but what rule 14a-8 required. The statements were laid down very much as ipse dixit, neither authority nor reasoning being advanced in their support. The court’s purpose in making these statements was primarily to set a tone: stockholders should consider themselves lucky that the SEC adopted rule 14a-8 and should not carp at their benefactor’s techniques of dispensation. It may also be relevant that Dyer was apparently a rather litigious individual whom the Eighth Circuit openly regarded as vexatious, not to say irritating. See Dyer v. SEC, 289 F.2d 242, 244-45 (8th Cir. 1962); Dyer v. SEC, 287 F.2d 773, 775-77, 782 (8th Cir. 1961); Dyer v. SEC, 266 F.2d 33, 37, 46 (8th Cir. 1959). See also Dyer v. SEC, 291 F.2d 774 (8th Cir. 1961); Dyer v. SEC, 290 F.2d 524 (8th Cir. 1961).

130 227 Ore. at 404, 405, 362 P.2d at 768.
131 Id. at 406, 362 F.2d at 769.
corporations! Ironically, the Carter court itself found the proposal at issue to be improper for shareholder action, thus bellying its claim to need an administrative predetermination of the propriety question.

Apart from the opinion’s confusion, moreover, there does exist an organ, albeit imperfect, which is capable of making a “preliminary determination that a stockholder’s proposal is a ‘proper’ one”—management, acting on the advice of corporate counsel. In the first instance, that is to say, a shareholder proposal is not filed with a court but submitted to the corporation. If management determines that it concerns a proper subject, that will end the matter. Only if management determines that it does not concern a proper subject will a court be faced with the shareholder’s challenge to management’s position. In determining whether a proposal concerns a proper subject, a judge would not be tilling unplowed soil, as the Oregon court seemed to believe, since he would be guided by a number of SEC administrative decisions, the thinking of many commentators, and even decisional law. Furthermore, in most cases corporate proceedings would not have to be delayed pending decision on the shareholder challenge, unless of course the requirements of a preliminary injunction were met and a court found management’s action so egregiously wrong that such an injunction should issue.

Finally, although the Carter court indicated some concern with the shareholder-harassment strawman propped up by the defendants, few shareholders and even fewer attorneys would be willing to invest their time, effort and dollars in frivolous, contentious litigation of this kind. In sum, then, those who

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124 See the commentaries at note 133 supra.


126 Since such litigation does not aim at a recovery from management, or any recovery at all, it would not normally lend itself to strike suits.
would deny shareholder access to the corporate proxy materials for the purpose of including a proposal which is within the shareholder competence to initiate and act upon, should be required to furnish a court with more than the Carter opinion if their position is to carry the day.\footnote{Access to the proxy materials for purposes of making a proposal, like access for the purpose of designating candidates for office, may be limited by reasonable bylaws. See notes 77–78 \textit{supra}. Even if not so limited, such access would not be impracticable. Proxy Rule 14a-8(a), 17 C.F.R. § 240.14a-8(a) (1969), has long required inclusion of most stockholder proposals in the proxy materials for annual meetings of corporations subject to the rules, with no discernible practicability problems. The shareholders’ right under state law to include proper nonelection proposals in proxy statements would extend also to special meetings, but under the state statutes special shareholders’ meetings can normally be called only by some minimum percentage of the shareholders, usually a fairly high percentage, see, e.g., \textit{Cal. Corp. Code} § 2202(c) (West 1955) (twenty percent of the voting power); \textit{Ohio Rev. Code Ann.} § 1701.40(a)(3) (Page 1964) (twenty-five percent, unless charter specifies otherwise); or by the board and by such other persons as may be authorized by the certificate or bylaws, see \textit{Del. Code Ann. tit. 8, § 211(d) (Supp. 1968)}; \textit{N.Y. Bus. Corp. Law} § 602(c) (McKinney 1953), \textit{as amended}, (McKinney Supp. 1969). Consequently, the proxy machinery could not be used for shareholder proposals between annual meetings unless the proposal was being made by the number of shareholders entitled to call for a special meeting.}{137}

\textbf{(b) Reimbursement of Expenses.} — Assuming that shareholders are entitled to place a proper nonelection proposal in the corporate proxy statement and proxy card, the question arises whether they should be reimbursed for the expense of follow-up techniques used to solicit votes for the proposal. This problem is analogous to that posed by the reimbursement of insurgent campaign expenses. Strict application of the relevant principles might seem to indicate that shareholders should be reimbursed\footnote{See \textit{p. 1512} \& note 92 \textit{supra}.}{138} subject only to the restrictions imposed on the board in such cases\footnote{See pp. 1518–19 \textit{supra}.}{139} But permitting shareholders to engage in follow-up techniques at the expense of the corporation might tend to deplete unduly the corporate treasury. If a shareholder were required to provide initially the necessary funds for such techniques, both the number of shareholders employing such techniques and the amounts expended would undoubtedly be limited. Yet, if a shareholder could rely on an absolute right of reimbursement, it is questionable whether the necessity to provide initial capital would be a sufficient check. The preferable rule would thus appear to be one analogous to that adopted for insurgent campaign expenses: That shareholders do not have a right to be reimbursed for follow-up expenses in nonelection proxy solicitations, but that the corporation acting through its shareholders has the power to reimburse such expenses, at least to the extent that comparable
expenses have been incurred in advancing comparable proposals.

2. Counter-Arguments to Management Proposals. — A related problem is whether shareholders have access to the corporate proxy materials in order to argue against nonelection proposals submitted by management. Since rule 14a-8 expressly excludes counter-proposals, this question is strictly one of state law.

Assuming that shareholders have access to the corporate proxy machinery for the purpose of submitting proposals which are within their authority to initiate, access for the purpose of arguing against nonelection proposals submitted by management would not be necessary for the effectuation of the shareholders' legal powers. Such access might nevertheless be useful. Although nonelection proposals do not involve an inherent self-interest on management's part, it is nevertheless true that they often involve self-interest in fact. Shareholder access to the corporate proxy machinery for the purpose of arguing against such proposals would help insure that such conflicts, and the proposals themselves, were fully explored. On the other hand, the absence of such access does not necessarily lead to a one-sided picture. A duty to disclose in the proxy materials all material facts relevant to a management proposal is imposed on management itself by state law, by the Proxy Rules (if the solicitation falls under

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140 Rule 14a-8(a), 17 C.F.R. § 240.14a-8(a) (1969). The counter-proposal exception was adopted in 1967. In the previous year the SEC had issued a press release requesting comments from the public on a series of proposed amendments to various Proxy Rules, including rule 14a-8. SEC, Securities Exchange Act of 1934 Release No. 8000, at 3–4, 13–14, 31 Fed. Reg. 15750–51, 15753–54 (1966). Nothing was said in this release concerning the possibility of adding a counter-proposal exception to rule 14a-8, and no notice was ever given that such an amendment was being contemplated. Nevertheless, such an amendment was included when the SEC published a final version of the amendments it had proposed in 1966. SEC, Securities Exchange Act of 1934 Release No. 8206, 32 Fed. Reg. 20960, 20961, 20964 (1967). The release gave no reason for the exception. Id. at 20961.

It might be noted that section 4(b) of the Administrative Procedure Act, 5 U.S.C. § 503(a) (1964), provides: "General notice of proposed rule making shall be published in the Federal Register . . . and shall include . . . either the terms or substance of the proposed rule . . . . [T]his subsection shall not apply to interpretative rules . . . ." In response to a question concerning the procedure by which the counter-proposal amendment was adopted, the Commission replied:

This amendment was included in the adopted proposals on the basis that it was merely a codification of the proper interpretation of Rule 14a-8 and therefore involved no substantial change in the rule. The reason for this position is that counter proposals are, in effect, a solicitation of a vote against the management's proposal.


141 See p. 1518 supra; Eisenberg, supra note 2, at 27–33.

142 See cases cited in note 13 supra.
those Rules), and by rule 1ob-5 (if the proposal is "in connection with the purchase or sale of any security"). Failure to make the necessary disclosure may not only be a ground for setting aside the action taken pursuant to the solicitation, but may result in civil or even criminal liability. When the solicitation falls under the Proxy Rules, the disclosure obligation is also backed up by administrative review of the proposed proxy materials.

Furthermore, shareholder access for the purpose of arguing against management proposals would raise substantial problems of feasibility. Since shareholders frequently could not be expected to anticipate a management solicitation relating to a non-election proposal, such access would often require a second round of proxy materials, entailing not only substantial expense, but substantial delay. Particularly where the management proposal concerns an action to be taken in conjunction with another business enterprise, as in the case of a merger or a sale of substantially all assets, such delay might prove intolerable.

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