ARTICLES

QUIETING THE SHAREHOLDERS' VOICE: EMPIRICAL EVIDENCE OF PERVASIVE BUNDLING IN PROXY SOLICITATIONS

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ABSTRACT

The integrity of shareholder voting is critical to the legitimacy of corporate law. One threat to this process is proxy "bundling," or the joinder of more than one separate item into a single proxy proposal. Bundling deprives shareholders of the right to convey their views on each separate matter being put to a vote and forces them to either reject the entire proposal or approve items they might not otherwise want implemented.

In this Paper, we provide the first comprehensive evaluation of the

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anti-bundling rules adopted by the Securities and Exchange Commission ("SEC") in 1992. While we find that the courts have carefully developed a framework for the proper scope and application of the rules, the SEC and proxy advisory firms have been less vigilant in defending this instrumental shareholder right. In particular, we note that the most recent SEC interpretive guidance has undercut the effectiveness of the existing rules, and that, surprisingly, proxy advisory firms do not have well-defined heuristics to discourage bundling.

Building on the theoretical framework, this Article provides the first large-scale empirical study of bundling of management proposals. We develop four possible definitions of impermissible bundling and, utilizing a data set of over 1,300 management proposals, show that the frequency of bundling in our sample ranges from 6.2 percent to 28.8 percent (depending on which of the four bundling definitions is used). It is apparent that bundling occurs far more frequently than indicated by prior studies.

We further examine our data to report the items that are most frequently bundled and to analyze the proxy advisors' recommendations and the voting patterns associated with bundled proposals. This Article concludes with important implications for the SEC, proxy advisors, and institutional investors as to how each party can more effectively deter impermissible bundling and thus better protect the shareholder franchise.

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INTRODUCTION

The shareholders' franchise to vote provides the ideological underpinning that "legitimates the exercise of power by some (directors and officers) over vast aggregations of property that they do not own."[1] While historically both state and federal law protected the legitimacy of corporate voting, beginning in 1934 with the passage of Section 14 of the 1934 Exchange Act, federal law has taken the laboring oar in safeguarding shareholders' voting rights.[2] In particular, Section 14 constructs an elaborate regulatory framework around the format, content, and timing of proxy statements and proxy cards that public companies send to their investors in preparation for their shareholder meetings to elect directors and to vote on other corporate matters requiring shareholder approval. The animating philosophy behind Congress's enactment of Section 14 and the

1. Blasius Indus., Inc. v. Atlas Corp., 564 A.2d 651, 659 (Del. Ch. 1988). Shareholders have few rights and the few they enjoy are deeply qualified. *See, e.g.*, Lucian A. Bebchuk, *The Myth of the Shareholder Franchise*, 93 VA. L. REV. 675, 676 (2007); Julian Velasco, *The Fundamental Rights of Shareholders*, 40 U.C. DAVIS L. REV. 407, 407 (2006). Nonetheless, the right to vote, whether in the election of directors or matters that corporate law requires at least the consent of the shareholders, is foundational to the governance model of the modern public corporation. For an insightful review of different views of the purpose behind the power to vote, see Robert B. Thompson & Paul H. Edelman, *Corporate Voting*, 62 VAND. L. REV. 129, 145–52 (2009) (embracing the important role of shareholder voting based on "error correction" in the firm's stock price while rejecting other theories, including that voting addresses the "incomplete contract" problems in business settings).

2. *See, e.g.*, 2 JAMES D. COX & THOMAS L. HAZEN, COX & HAZEN ON CORPORATIONS § 13.30 (3d ed. 2010).

SEC's proxy rules is that shareholders need to be fully informed about all of the matters on which corporate law requires their approval. Indeed, the proxy rules are central to governance of public companies.

In 1992, the SEC greatly strengthened the shareholder franchise through a suite of amendments to the proxy rules.[3] Among the changes introduced by the 1992 amendments were two rules, referred to as the "Unbundling Rules,"[4] that prohibit companies from "bundling" together multiple voting items into a single proposal with a single box on the proxy card. The SEC's rules target such bundled proposals since they distort shareholder choice, and thereby disenfranchise shareholders. Bundling has another harmful effect: joining in one resolution two distinct substantive items has the necessary effect of preventing shareholders from expressing their views to directors on each matter being put to a vote. In other words, the joinder of unrelated substantive items causes shareholders to approve items that they might not otherwise want implemented and also robs the directors of awareness of the shareholders' views on each bundled proposal. While these basic principles are easily stated, in practice the rules have been difficult to implement and, as developed below, have been further muddled by SEC interpretations that lack the support of both the SEC's initial regulatory guidance on bundling and the relevant case law.

In this Paper we provide the first comprehensive evaluation of the SEC's Unbundling Rules. We begin in Part I with a discussion of the corporate governance framework where we see that management enjoys numerous practical and legal strategic advantages. These advantages are in stark contrast with the prevalent "nexus of contracts" perspective of corporate law where consent by owners is a central cog in the governance wheel. The perspective gained in this discussion underscores the importance of the shareholder vote, a matter that is directly implicated by the practice of bundling.

In Part II of the Paper, we provide a careful dissection of the rules themselves as well as a close analysis of their interpretation by the courts

3. In addition to addressing bundling, the SEC also acted to address how regulation contributes to the collective action problem among investors in public companies. *See* Regulation of Communications Among Shareholders, Exchange Act Release No. 31,326, 57 Fed. Reg. 48,276 (Oct. 22, 1992) (to be codified at 17 C.F.R. pts. 240, 249) [hereinafter Communications Release] (adopting a wide number of amendments to the proxy rules with the cumulative effect of enabling greater freedom to interact among shareholders and their advisors in connection with proxy voting). These sweeping changes were first proposed in Regulation of Communications Among Securityholders, Exchange Act Release No. 30,849, 57 Fed. Reg. 29,564 (proposed July 2, 1992) (to be codified at 17 C.F.R. pts. 240, 249) [hereinafter Communications Among Securityholders].

4. Exchange Act Rules, 17 C.F.R. §§ 240.14a-4(a)(3), (b)(1) (2014).

and the SEC. We find that the courts have carefully developed several interpretative approaches to define impermissible bundling. In contrast, we show that the SEC's approach to its own rules has become less vigorous and, as we ultimately conclude, inconsistent with the goals it announced for the rules when they were adopted. Indeed, we conclude that the SEC interpretive guidance has undercut the effectiveness of the existing rules and created unnecessary ambiguity about their proper application.

We conclude Part II with an examination of the voting policies of third party voting advisors that counsel investors how to vote on proxy proposals. We find that, surprisingly, these advisors have not developed any analytical structures for dealing with bundled proposals. We examine the voting policies of the two major voting advisors, Institutional Shareholder Services ("ISS") and Glass Lewis. We find each has failed to provide clear advice to their clients to vote against bundled proposals. Instead of operating from well-developed heuristics for detecting harmful bundling, the advisors act on an ad hoc basis, applying balancing tests to determine whether the bundled proposals predominantly benefit or harm shareholders, with the end result being muddled outcomes.

In Part III, to illustrate the spectrum of possible definitions of impermissible bundling, we offer four possible classifications of bundling. The four types range from the broadest to the most narrow: (1) any proposal with more than one item[5] (we refer to this as "generic bundling"); (2) any proposal with more than one item, where at least one of those items is material ("material bundling"); (3) any proposal with more than one item, where two or more of those items are material ("multiple material bundling"); and (4) any proposal with more than one item, where at least one of those items is material and negatively affects shareholders rights ("negative bundling"). We also provide various examples of egregious bundling to highlight the importance of this problem.

Part IV of the Paper applies our four potential tests to a large sample of actual shareholder votes to determine the prevalence of bundling under our alternative definitions. Under each of these definitions, we find that companies engage in impermissible bundling far more frequently than indicated by prior research. Using a ten-year data set containing a total of 1,349 management proposals, we find some form of bundling was present in 28.8 percent of those proposals, while nearly 80 percent of the bundling

5. Across the four definitions, by "more than one item" we mean "more than one substantively different item." That is, we would not consider a substantively single item with multiple components to be a case of bundling.

uncovered involved multiple items with a material impact on the shareholders.

Next, in Part V, we examine shareholder voting on bundled proposals. In particular, we provide empirical evidence for how proxy advisors respond to bundling, their recommendations in connection with bundled proposals, and how shareholders vote on bundled proposals. These data provide more insight on the response of proxy advisors to bundling and the impact of proxy advisors' recommendations.

We conclude in Part VI with a discussion of the policy implications of our findings. We provide specific recommendations for both the SEC and the third party voting advisors so that the pervasive bundling practice we report here can be addressed and the shareholder franchise can be liberated from the chains of bundling.

I. SHAREHOLDERS' VOICE vs. MANAGEMENT'S STRATEGIC ADVANTAGES IN TODAY'S CORPORATE FRAMEWORK

Abuses of shareholders' voting rights led to the adoption of Section 14 of the 1934 Exchange Act.[6] Congress's action "stemmed from the congressional belief that '[f]air corporate suffrage is an important right . . . .' It was intended to 'control the conditions under which proxies may be solicited with a view to preventing the recurrence of abuses which . . . [had] frustrated the free exercise of the voting rights of stockholders.'"[7] Over the ensuing decades, the SEC has been vigilant in protecting shareholder voting rights against potential managerial abuses.

In addition to the election of directors, for which SEC rules strictly proscribe bundling,[8] shareholder voting customarily arises in three important areas: charter and bylaw amendments, transactions involving acquisitions, and executive compensation.[9] Without diminishing the

6. COX & HAZEN, *supra* note 2, at 545.

7. J. I. Case Co. v. Borak, 377 U.S. 426, 431 (1964) (quoting H.R. REP. NO. 73-1383, at 13–14 (1934)).

8. In contrast to the approach in the Unbundling Rules—which generally prescribe separate votes for each separate matter and naturally lead to questions as to what is a separate matter—the SEC proxy rules take a more definitive approach. In the election of directors, to prevent multiple nominees to the board being subject only to a single vote, the SEC proxy rules provide that the proxy form must include a means by which voting shareholders can withhold their vote from *any* director. 17 C.F.R. § 240.14a-4(b)(1). The rules then set forth three distinct nonexclusive means for shareholders to withhold their vote. § 240.14a-4(b)(2).

9. *See* Paul H. Edelman et al., *Shareholder Voting in an Age of Intermediary Capitalism*, 87 S. CAL. L. REV. 1359, 1367–68 (2014). While there are a variety of other situations that involve shareholder voting, they are not important for our purposes because they are unlikely to implicate the

importance of the shareholder voice in approving an acquisition[10] or executive compensation,[11] our study focuses on amendments to either the charter or the bylaws because, in the contemporary legal context, the charter and the bylaws are what define the shareholders' relationship to the firm. As the next section develops, meaningful shareholder consent is central to the modern perspective of the public company. To this end, the Unbundling Rules were adopted by the SEC to protect the exercise of that consent.

A. NEXUS OF CONTRACTS IDEOLOGY

The most important perspective that shapes corporate law today is the view that the corporation is a "nexus of contracts." Building on Ronald Coase's perspective on why firms exist (labor, suppliers, customers, investors, and managers arrange their activities to their optimal benefit),[12] leading legal scholars, and in turn practitioners, embrace private ordering as the desired norm within corporate law. In a world of private ordering, the state corporate statute is understood to have the limited role of providing default rules in those instances where the parties have not otherwise specified how their affairs or activities are to occur.[13]

Frank Easterbrook and Daniel Fischel were early advocates for viewing corporate law as consensual. Much of their embrace of the nexus of contracts theory was based on their belief that it is necessary for business

issues discussed in this paper (for example, shareholder initiated votes using Rule 14a-8, mandatory say-on-pay votes, or contested elections which involve single items with a single voting box on the ballot).

10. Shareholder voting is also important for some types of M&A activity. For instance, under state corporate law, mergers and consolidations require shareholder approval by both companies involved in the transaction. *See, e.g.*, DEL. CODE ANN. tit. 8, § 251(c) (2016); MODEL BUS. CORP. ACT § 11.04(d) (AM. BAR ASS'N 2007). There are exceptions to these mandatory voting requirements for the shareholders of an acquiring company in a small-scale merger. *See, e.g.*, DEL. CODE ANN. tit. 8, § 251(f); MODEL BUS. CORP. ACT § 11.04(g). More narrowly, sales of all or substantially all of the assets of a corporation require the approval of only the selling corporation's shareholders. *See, e.g.*, DEL CODE ANN. tit. 8, § 271; MODEL BUS. CORP. ACT § 12.02. There are also exceptions for shareholders of a subsidiary corporation when the acquirer invokes the short-form merger process. *See, e.g.*, DEL. CODE ANN. tit. 8, § 253 (requiring at least 90 percent ownership by parent); MODEL BUS. CORP. ACT § 11.05 (same).

11. In the executive compensation area, shareholder voting is necessary for most stock option plans. *See* Randall S. Thomas & Kenneth J. Martin, *The Determinants of Shareholder Voting on Stock Option Plans*, 35 WAKE FOREST L. REV. 31, 47–48 (2000).

12. *See generally*, R. H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386 (1937).

13. *See, e.g.*, Frank H. Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416, 1426 (1989) (referring to the corporation as a "nexus of contracts," which "is just short hand for the complex arrangements of many sorts that those who associate voluntarily in the corporation will work out among themselves").

enterprises to be "adaptive" because organizations, and their actors, are buffeted by an ever-changing business environment.[14] Businesses, they argued, are dynamic entities best served by adaptive actors. From this perspective, it is natural to conclude that the law should accommodate this reality. To this end, they reason that owners and managers must be able to tailor their relationship to ever-changing circumstances. To nexus of contracts adherents, corporate rules are not mandatory, but default rules; the parties are free to tailor the relationship to their own particular needs.[15]

Pursuant to this view, corporate law as provided by the state is merely facilitative of private bargaining—corporate law is not public, but private law. In such a realm, the only issue in doubt is what constitutes consent among the affected parties; after all, the consent that Coase and contract theory so heavily depend upon as the basis for the efficiency is the outcome of bargaining.

Because consent is a necessary feature for the contractual paradigm and therefore is foundational to corporate law today, the efficacy of proxy voting is of great import; simply stated, because a contract arises when and only when there is a meeting of the minds on the parties' respective undertakings, choice, both free and informed, is central to the relationship owners have to their corporation.[16] The best way to insure that the shareholders consent to entering into, or altering, the corporate contract is by seeking their fully informed approval of that contract or any changes to it. Informed shareholder voting is an obvious solution to the question of how to obtain such consent.[17]

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14. *See id*. at 1428.

15. *See id*. at 1434–36.

16. Consent and contracting can be found within the shareholder's relationship to the corporation; but that relationship is richer and potentially more fluid than contractual relationships because of a set of governance arrangements and procedures that permeate corporate statutes and thereby define corporate organizations. *See, e.g.*, Lawrence A. Hamermesh, *Consent in Corporate Law*, 70 BUS. LAW. 161, 162 (Winter 2014/15) (arguing that consent is also a necessary component of governance). Consent can be found at the moment the shareholder purchases shares in the corporation; the transaction is bound by consideration on the part of the corporation and the shareholder, and the terms of their bargain are set forth in the laws of the state of incorporation, the articles of incorporation, and the bylaws. Thereafter, changes in this contract can be understood to occur when the state of incorporation amends its corporate statute, the corporation amends its articles of incorporation, or the bylaws are amended.

17. Recent decisions in Delaware, although invoking the nexus of contracts approach, have invited close scrutiny of what constitutes consent as well as the soundness of the nexus of contracts perspective. In *Boilermakers Local 154 Retirement Fund v. Chevron Corp.*, Chancellor Strine held that the board acting without the consent of the shareholders could nonetheless adopt a bylaw provision that permitted the corporation to choose the forum in which a shareholder-initiated suit would be maintained. Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934, 939 (Del. Ch. 2013).

B. RELATIVE BARGAINING POWER OF SHAREHOLDERS AND MANAGERS

Inside this contractual framework, management, not the shareholders, enjoys a significant strategic advantage within the dynamics of the corporate web within which the shareholder contract exists. It is this point that raises our concern for bundling. Consider that the corporate documents are the supreme source of the contract that exists between the corporation and its shareholders. Shareholders and managers, however, do not approach changes in the charter or bylaws on the same footing.

1. Charter Amendments

Any change to the corporate charter must first be proposed by the board of directors[18] so that the shareholders' role is reactive, not proactive, in shaping the change that is proposed. Because of this, management enjoys a strategic advantage over shareholders in controlling the timing, details, and information that surrounds the proposal.[19] Further adding to the power

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This decision was followed by *ATP Tour, Inc. v. Deutscher Tennis Bund* where the Delaware Supreme Court, relying on the reasoning in *Boilermakers*, upheld a board-adopted bylaw concerning litigation costs that abandoned the long-maintained "American Rule" whereby litigants bear their own costs, and instead made the plaintiff bear the defendant's expenses—which would include the corporation's costs in a derivative suit—unless the plaintiff prevailed. ATP Tour, Inc. v. Deutscher Tennis Bund, 91 A.3d 554, 558 (Del. 2014). *Boilermakers* and *ATP Tour* each reasoned from the perspective that the shareholders' relationship with the corporation, and in turn their relationship to the board of directors, is contractual so that much of the shareholders' rights can be understood to flow from certain organic documents, and most significantly and pervasively from the company's bylaws.

It is not our purpose here to question the force or legality of such unilateral action. Instead we invoke the controversy that has surrounded *Boilermakers* and *ATP Tour* as a testament of the importance society assigns to shareholder voting. As we noted earlier, in *Atlas*, former Chancellor Allen observed that it is the shareholders' voting franchise that provides the ideological underpinning that "legitimates the exercise of power by some (directors and officers) over vast aggregations of property that they do not own." Blasius Indus., Inc. v. Atlas Corp., 564 A.2d 651, 659 (Del. Ch. 1988). Building on this insight, we believe the results reached in both decisions would have been significantly less controversial, and likely not controversial at all, had the bylaws been adopted with the approval of the shareholders. Not only does such approval improve the optics of the transaction that otherwise can be seen as self-serving on the part of the directors (who are likely to be the targets of shareholder suits), but such approval would more easily fall within prevailing notions of governance while obtaining the type of consent on which the nexus of contracts paradigm invokes the least controversy. However, the data collected and analyzed in this study raises a good deal of disquiet regarding the vulnerability of the shareholder franchise. That is, our empirical analysis identifies many instances in which impermissible bundling likely distorted the outcomes of proxy votes—suggesting that even proposals adopted with shareholder consent may be controversial because self-interested managers can skew the voting process.

18. *See, e.g.*, DEL. CODE ANN. tit. 8, § 242(b)(1) (2016); MODEL BUS. CORP. ACT § 10.03(a) (AM. BAR ASS'N 2007).

19. Lucian A. Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 863 (2005) ("Management . . . has the sole power to put proposals on the table, and shareholders have to vote up or down on these proposals without having the option to amend them."). The power to set the agenda also enables management to obtain approval of measures which decrease shareholder value. *Id.*

imbalance is the well-known collective action problem that weakens the shareholders' voice.[20] Such concerns regarding the imbalance of power between managers and owners support the view that when interpreting the proxy rules, such as the Unbundling Rules, the potential of adverse consequences on the critical role of consent should be fully understood, so that at least when changes to the corporate charter are being proposed the imbalance is not exacerbated.

2. Bylaw Amendments

In contrast to corporate law's treatment of amending the charter, bylaws can be initiated by the shareholders as well as by the board of directors.[21] Nonetheless, a board acting to amend the bylaws enjoys three strategic advantages over shareholders who seek to change their relationship to the corporation through amending the bylaws.

The first two advantages are grounded in economic theory. To begin with, the informational advantages of those in control permit them not only to time a change to their own advantage, but to understand better than outside shareholders the full effects of a bylaw change they propose. As a consequence of their information advantages, managers are well positioned to act opportunistically to pursue self-interested ends of which only they can be fully aware. Second, insiders acting to amend bylaws do not face the formidable collective action problem that outside shareholders incur in moving a bylaw through the approval process. While both boards and shareholders enjoy the right to amend the bylaws, the board, being a cohesive body, as a practical matter enjoys lower costs and less uncertainty by choosing the bylaw course of action. Indeed, under corporate law, any cost related to board-initiated actions is borne by the corporation, whereas the shareholders' cost to act, and most importantly to persuade fellow shareholders, is borne by the activist shareholder.

Thirdly, the law tilts heavily against the shareholders in American public companies having the right to alter the fundamental structure of the corporation; corporate statutes set forth the basic structure of the corporation subject to countervailing provisions in the articles of incorporation. Thus, if there are changes from the default rule that corporate affairs are managed by or under the direction of the board of

at 865.

20. John C. Coates, IV, *Measuring the Domain of Mediating Hierarchy: How Contestable Are U.S. Public Corporations?*, 24 J. CORP. L. 837, 849 (1999) (closely examining weaknesses in shareholder voting due to the collective action problem).

21. DEL. CODE ANN. tit. 8, § 109; MODEL BUS. CORP. ACT § 10.20.

directors, the preferred structure must appear in the articles of incorporation. As discussed earlier, only the board of directors has the power to initiate amendments to the articles of incorporation.[22] This feature of American corporate law not only reduces the shareholders to a reactive role in defining their governance structure, but also necessarily restricts the area that is a proper subject for shareholder action.

The Delaware Supreme Court's holding in *CA, Inc. v. AFSCME Employees Pension Plan* illustrates this point.[23] Shareholders sought to include on management's proxy statement a bylaw whereby a non-management nominee who was elected to the board should be reimbursed for reasonable expenses incurred in that nominee's successful contest for office. The Delaware Supreme Court held that the shareholders' authority to amend the bylaws was limited to matters that are "procedural [or] process-oriented,"[24] meaning that bylaws that encroach upon the managerial authority of the board of directors would be inappropriate. This construction was based on the Delaware court providing that "[t]he business and affairs of every corporation . . . shall be managed by or under the direction of the board of directors, except as may be otherwise provided . . . in its certificate of incorporation."[25] If shareholders had the authority to initiate an amendment of the articles of incorporation, they would not be limited to "procedural [or] process-oriented" matters; they could initiate, as the board can initiate, a wide-range of substantive alterations to the conduct of the corporate affairs. Since shareholders lack authority in the very area that the board enjoys authority, the shareholders' prerogative to initiate is greatly constrained within a private-ordering environment; questions regarding the authority to change or opt out of a default rule will therefore not be found when it is the board acting to change the rules of the game rather than when the action is by the shareholders. It is for this reason that the nexus of contracts rubric necessarily threatens shareholder protection.

It is interesting to consider further the relative power of the shareholders and directors to alter the rules of governance. Even though the bylaw involved in *CA, Inc.* was deemed to be process and procedurally oriented, the court held the proposed bylaw was not appropriate for shareholder action because the proposed bylaw could *possibly* be interpreted to require reimbursement in instances that would be inconsistent

22. *See supra* note 18 and accompanying text.
23. CA, Inc. v. AFSCME Emps. Pension Plan, 953 A.2d 227 (Del. 2008).
24. *Id*. at 235.
25. *Id*. at 232 (citing DEL. CODE ANN. tit. 8, § 141(a)).

with the board's fiduciary obligations.[26] By contrast, in *Boilermakers Local 154 Retirement Fund v. Chevron Corp.*,[27] a pension fund challenged a board-adopted forum selection bylaw by raising multiple examples where the bylaw could be harmful to the corporation. Similar to *CA, Inc.*, the pension fund argued that this rendered the bylaw invalid. Chancellor Strine summarily dismissed that challenge on the ground that "it would be imprudent and inappropriate to address these hypotheticals in the absence of a genuine controversy with concrete facts."[28]

The contrasting rulings in *Boilermakers* and *CA, Inc.* have led some of the authors of this Article to question whether shareholder and board-initiated bylaws stand on the same footing:[29] a shareholder-initiated bylaw is subject to a threshold determination that the subject is organically of the type that is proper for shareholder action and is also subject to ex ante scrutiny for its *potential* inconsistencies with corporate law; in contrast, board-initiated bylaws escape such ex ante scrutiny.[30]

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26. *Id*. at 239–40. The Delaware Supreme Court reasoned that because the bylaw could be invoked by a candidate who sought office solely to advance personal, rather than corporate, interest, the bylaw was invalid.

27. Boilermakers Local 154 Ret. Fund v. Chevron Corp., 73 A.3d 934 (Del. Ch. 2013).

28. *Id*. at 940.

29. One of us has written a recent article making this point. James D. Cox, *Corporate Law and the Limits of Private Ordering*, 93 WASH. U. L. REV. 257 (2015).

30. The authors begin their analysis by observing that both the reimbursement bylaw in *CA, Inc.* and the forum selection bylaw in *Boilermakers* employed "shall" as the operative verb. *CA, Inc.*, 953 A.2d at 230 ("The board of directors *shall* cause the corporation to reimburse a stockholder . . . ." (emphasis added)); *Boilermakers*, 73 A.3d at 942 ("Unless the Corporation consents in writing, . . . the Court of Chancery . . . *shall* be the sole and exclusive forum . . . ." (emphasis added)). However, in the case of *CA, Inc*., the proposed bylaw mandated action by the board, whereas with *Boilermakers*, the bylaw was more broadly proscriptive in identifying the venue for suit, mandating suits be in the Court of Chancery unless the board exercised its discretion for a suit to be in another jurisdiction. However, that choice could only be made by the board if made in writing, so to this small extent there was some impact on how the board was to exercise its choice. In both cases, there were two distinct lines of attack on the bylaw: (1) whether the body adopting the bylaw had the authority to act on the subject matter; and (2) whether, assuming authority, the bylaw nonetheless was inappropriate because it could authorize later conduct that would be a violation of the directors' fiduciary obligation. *CA, Inc*. and *Boilermake*rs each answered the first question affirmatively, albeit using different approaches to justify the shareholder's authority in *CA, Inc*. and the board's authority to act in *Boilermakers.* What these authors find instructive here is the courts' divergence on the second issue due to the differing approaches towards bylaws initiated by the board and bylaws initiated by shareholders. This is evident in Chancellor (now Chief Justice) Strine's reasoning as to why the plaintiffs' "parade of horribles" did not render the forum selection bylaw invalid, whereas the imagined situation in *CA, Inc*. *did* render the reimbursement bylaw invalid:

> The plaintiffs try to show that the forum selection bylaws are inconsistent with law and thus facially invalid by expending much effort on conjuring up hypothetical as-applied challenges in which a literal application of the bylaws might be unreasonable. . . . [I]f a plaintiff believes that a forum selection clause cannot be equitably enforced *in a particular situation*, the plaintiff may sue in her preferred forum and respond to the defendant's motion to dismiss for

We are left with a conundrum in corporate governance. Shareholder consent is vital to the legitimacy of the corporate organization. However, shareholders are largely constrained in the exercise of their consent to reacting to management proposals. Moreover, these constraints occur in a practical and legal environment that heavily favor management—the customary initiator of the instances where shareholders vote. This suggests to us that the space in which the legitimizing voice of the shareholders dwells is both rare and hallowed and, therefore, worthy of the utmost protection. With this in mind, we next examine the scope and purposes of the Unbundling Rules as important safeguards to the shareholders' franchise to vote.

II. THE UNBUNDLING RULES

Shareholders' voting choices are necessarily distorted when management bundles multiple items into a single proposal on which it permits only one vote. For example, management may propose to the shareholders two charter or bylaw amendments for their approval. If instead of providing for separate votes on each amendment, the two distinct proposals are combined in a single resolution, the shareholders are robbed of expressing a distinct choice with respect to each because their joinder

> improper venue by arguing that, under *Bremen*, the forum selection clause should not be respected because its application would be unreasonable. The plaintiff may also argue that, under *Schnell*, the forum selection clause should not be enforced because the bylaw was being used for improper purposes inconsistent with the directors' fiduciary duties.

Boilermakers, 73 A.3d at 958 (footnote omitted) (emphasis added).

The question that arises from Chancellor Strine's reasoning is why this approach was not equally suitable for the broad bylaw before the court in *CA, Inc.* Since Chancellor Strine does not distinguish the cases by the operative language of the two bylaws, the distinction between the two opinions with respect to confronting the question of the bylaw's possible overreach can be seen as according bylaws initiated by the board with a presumption of propriety that is missing with bylaws adopted by the shareholders.

A possible counterargument to this point offered by one commentator on this Article is that there were differences in the language of the bylaws in the two cases: the bylaw in *CA, Inc.* was mandatory in all instances, whereas the bylaw in *Boilermakers* offered the board a limited avenue to exercise its discretion, suggesting that the different rulings might be attributed to the differences in the language of the bylaws.

One might believe that the contrasting approaches between *CA, Inc.* and *Boilermakers* are symptomatic of a larger problem with the architecture of corporate law, namely that the role and prerogatives of the board of directors is believed to be more clearly defined than the role and prerogatives of shareholders. *See* Velasco, *supra* note 1, at 430–34. However, because corporate statutes are areas where the shareholders enjoy protected rights that are defined with a good deal of precision, it would appear the problem is not a lack of precision but rather too much. As a result, the board, whose authority is broadly stated, enjoys unrestrained deference, whereas shareholders, whose rights are precisely defined, have erroneously not been accorded similar deference by the courts when they have mediated conflicts between the broad grant of authority to the board and more selective grants to the shareholders.

means the package must be approached by the shareholders as an all-up or all-down vote. The problem becomes most invidious when management attempts to "sweeten" one proposed anti-shareholder rights amendment by combining it with a second pro-shareholder amendment. Thus, shareholders may either accept the good with the bad (the proverbial spoonful of sugar to help the sour medicine go down), or reject both. This presents a distorted choice to shareholders. Not surprisingly, these efforts have been controversial.

The problem of bundling was well known in the 1980s when public companies regularly proposed to recapitalize by converting to a dual class common stock structure.[31] During that era, proposals would combine a small immediate dividend payment with changes to the voting structure of the company that entrenched managers by providing them with controlling voting rights in the firm.[32] Despite the long-term negative impact on shareholders, such recapitalizations were generally approved by shareholders because they were willing to forego uncertain greater future returns in the form of a potential takeover premium for the certainty of an immediate payout.[33] Certainly if both the special distribution and the recapitalization benefitted shareholders, there would have been no need for their joinder as each would have been approved independently if voted on separately. Their joinder, however, provided assurance to management that the bitter (entrenchment device) would be swallowed with the sweet (cash payout). Although midstream dual class recapitalizations largely disappeared by the mid-1990s,[34] bundling continued to be an issue for

31. In a typical recapitalization to dual class common stock, a firm would offer incentives (maybe a special dividend) to investors holding shares of the company's common stock to accept lower-tier, often non-voting, stock. These "midstream" recapitalizations were often followed by large decreases in the value of shares (due to the entrenching effects of dual class shares where voting shares are held by management). *See* Jeffrey N. Gordon, *Ties That Bond: Dual Class Common Stock and the Problem of Shareholder Choice*, 76 CAL. L. REV. 1, 3–4 (1988).

32. *Id*. at 48 ("Management can 'sweeten' a proposal that decreases shareholder wealth by bundling it with an unrelated proposal that increases wealth[,] . . . complicat[ing] the shareholder choice problem considerably and in the end distort[ing] the choice in management's favor.").

33. Gordon rejects the claim that by approving a sweetened proposal, shareholders and management have simply engaged in a mutually beneficial exchange leading to a Pareto improvement. *Id*. at 49. He argues that the presence of a significant insider bloc creates a scenario in which management need only convince a sufficiently large minority of public shareholders to accept the proposal in order for it to be approved. *Id*. By contrast, with no insider bloc, at least half of the public shareholders would have to approve the measure. *Id*. Further, by sweetening proposals with difficult-to-value provisions, management can achieve that sufficiently large minority relatively easier than with an easy-to-value sweetener because estimations as to value of the sweetener will be more dispersed. *Id.* Gordon notes that "[i]n this way, a sweetener operates less as a basis for a trade and more as a means for distorting shareholder choice." *Id.*

34. For one, the SEC adopted a rule prohibiting it in 1988, although that law was overturned in

shareholders.

In 1992, the SEC acted to prohibit the "electoral tying arrangements that restrict shareholder voting choices."[35] It promulgated Rule 14a-4(a)(3), which states that "the form of proxy [s]hall identify clearly and impartially *each separate matter* intended to be acted upon, whether or not related to or conditioned on the approval of other matters . . . ."[36] Further, Rule 14a-4(b)(1) requires that shareholders must be given "an opportunity to specify by boxes a choice between approval or disapproval of, or abstention *with respect to each separate matter* referred to therein as intended to be acted upon."[37] In its Adopting Release, the SEC explained that the two rules serve a dual purpose: to "permit shareholders to [(1)] communicate to the board of directors their views on each of the matters put to a vote, and [(2)] not be forced to approve or disapprove a package of items and thus approve matters they might not if presented independently."[38] Thus, since at least 1992, federal law has required that discrete proposals be voted on separately.[39]

A. BUNDLING IN THE COURTS

Since the adoption of the Unbundling Rules, there have been two key judicial decisions interpreting the rules: *Koppel v. 4987 Corp.*[40] and *Greenlight Capital, L.P. v. Apple, Inc.*[41] Both of these cases provide important guidance regarding the rules' purpose, scope, and application.

1. *Koppel v. 4987 Corp.*

In *Koppel*, the complaint alleged that a shareholder vote on the possible sale of a closely-held firm violated the Unbundling Rules because

court two years later. Stephen M. Bainbridge, *The Short Life and Resurrection of SEC Rule 19c-4*, 69 WASH. U. L.Q. 565, 566–67 (1991). By 1994, the major stock exchanges had all adopted rules prohibiting the practice. *Id*. at 626. *See also* Lucian A. Bebchuk & Ehud Kamar, *Bundling and Entrenchment*, 123 HARV. L. REV. 1549, 1558 (2010).

35. Communications Release, *supra* note 3, at 48,287.

36. Exchange Act Rule, 17 C.F.R. § 240.14a-4(a)(3) (2014) (emphasis added).

37. *Id.* § 240.14a-4(b)(1) (emphasis added).

38. Communications Among Securityholders, *supra* note 3, at 29,566.

39. *But see* Bebchuk & Kamar, *supra* note 34, at 1559 n.26. Bebchuk and Kamar claim that, because the Unbundling Rules allow for votes on one proposal to be contingent upon the results of another vote, they are too weak to prevent bundling. *Id*. They state that "[t]he unbundling rule permits management to condition the adoption of one proposal on the approval of another proposal. The rule requires only that shareholders be able to vote on the proposals separately—even if the approval of only one means that neither is implemented." *Id.*

40. Koppel v. 4987 Corp., 167 F.3d 125 (2d Cir. 1999).

41. Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716 (S.D.N.Y. Feb. 22, 2013).

the proxy card provided for a single up-or-down vote on three issues: (1) forbearance from terminating a net lease on a piece of property, (2) the sale of said property, and (3) distribution of the proceeds from the sale of the property.[42] While the plaintiff supported the sale of the property, he opposed the proposed distribution of proceeds scheme. He therefore challenged under the Unbundling Rules the two items being combined in a single resolution submitted to the shareholders. He argued that a single up-or-down vote meant that the shareholders' choice was distorted as they would have to vote to forego the sale of the building entirely or vote to accept an unfair distribution scheme.[43]

To reach the merits, the Second Circuit first addressed whether an implied private right of action existed for the Unbundling Rules, an issue of first impression. Building upon the Supreme Court's earlier recognition of the implied right of action under Rule 14a-9 for material misleading proxy statements,[44] the Second Circuit held there was an implied right of action for bundling, reasoning that "[i]mpermissible grouping of voting items frustrates fair corporate suffrage and the voting rights of shareholders no less than a misrepresentation or omission in a proxy."[45] The Second Circuit emphasized the harm of bundling by observing in its recognition of a private action that "not permitting such an action 'would be demonstrably inequitable to a class of would-be plaintiffs with claims comparable to those previously recognized.'"[46] The court further reasoned that private enforcement of the Unbundling Rules was needed to augment SEC enforcement efforts.[47]

On the merits of the claim, the court found that the Unbundling Rules required that "separate matters" be put to separate votes.[48] The court emphasized that the SEC's Adopting Release "suggest[ed] a strong preference for more voting items rather than fewer" when deciding whether items were separate matters from one another.[49] The court stated that "the SEC recognized that the new rules were specifically intended to

42. *Koppel*, 167 F.3d at 134.

43. *Id*.

44. *See* J. I. Case Co. v. Borak, 377 U.S. 426, 430–31 (1964).

45. *Koppel*, 167 F.3d at 135–36.

46. *Id.* at 136 (quoting Va. Bankshares, Inc. v. Sandberg, 501 U.S. 1083, 1104 (1991)).

47. *Id.* ("[W]e first note that the SEC has made clear through its submissions to this Court that it 'needs private actions as a supplement to its efforts to enforce Rule14a-4's separate matter requirement due to its limited staff resources.'" (quoting Letter from Harvey J. Goldschmid, Sec. Exch. Comm'n Gen. Counsel, to Lucille Carr, Operations Manager, U.S. Court of Appeals for the Second Circuit (Nov. 18, 1998))).

48. *Id.* at 138.

49. *Id.* (citing Communications Release, *supra* note 3, at 48,287).

'"unbundle" management proposals' and that those individual voting items may well constitute closely related matters."[50] The court further observed that this edict should be all the more palatable to management because SEC rules expressly provided that management could still condition one proposal on the approval of another.[51] Absent state corporation law on point, the court held that the actual issue of what constitutes a "separate matter" for purposes of the two rules is ultimately a question of fact to be determined in light of the corporate documents and in consideration of the SEC's apparent preference for more voting items rather than fewer.[52]

In the years following *Koppel* there were few cases invoking the Unbundling Rules;[53] much of the guidance on their interpretation was ultimately provided in the 2013 decision in *Greenlight Capital*.[54]

2. *Greenlight Capital, L.P. v. Apple, Inc.*

In *Greenlight Capital*, a hedge fund, seeking a means for Apple to distribute a portion of its significant cash, mounted a campaign to convince Apple, Inc. to issue perpetual preferred shares invoking the board's "blank check" authority (such a provision is more commonly referred to as "blank *stock*" authority, the convention we employ here except when drawing directly on the reasoning of *Greenlight Capital*).[55] Apple's board rejected the proposal and thereupon sought a shareholder vote to amend its corporate charter to remove the Apple board's blank check authority.[56] In seeking this amendment, Apple packaged in a single resolution the charter amendment that would remove the blank check authority with three other charter amendments: (1) adding a majority voting provision for the election of incumbent board members in uncontested elections, (2) establishing a nominal par value for Apple's stock, and (3) eliminating certain obsolete charter provisions.[57] Greenlight called foul and filed suit alleging that a

50. *Id.* (quoting Communications Release, *supra* note 3, at 48,287).

51. *Id.* at 138.

52. *Id.* The court was careful to point out that it was not deciding the merits of the anti-bundling rule violations, but merely stating that the claim should not have been dismissed under Rule 12(b)(6). *Id.* at 138–39. The case was remanded for further proceedings and was litigated before a jury. The jury returned a verdict for the defendants. *See* Greenberg v. Malkin, 39 F. App'x 633, 633 (2d Cir. 2002).

53. *See, e.g.*, Complaint at 5–7, MacCormack v. Groupon, Inc., No. 1:13-cv-00940-GMS (D. Del. May 24, 2013), http://securities.stanford.edu/filings-documents/1050/GRPN00_03/2013524_f01c_13CV00940.pdf.

54. Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716 (S.D.N.Y. Feb. 22, 2013).

55. *Id*. at *5–6.

56. *Id*.

57. *Id*. at *4.

single vote on all three items violated the Unbundling Rules.[58]

Apple offered five defenses: (1) the proposed voting item had only one matter for consideration—whether or not to amend the articles, (2) it was common proxy practice to package multiple amendments into a single item, (3) the proxy statement was not challenged by the SEC, (4) the voting item did not group more than one item which had a substantial effect on shareholder rights, and (5) the proposed provisions were pro-shareholder.[59] The first three defenses were easily rejected,[60] but the fourth and fifth claims were more significant.

In the fourth defense, Apple claimed that the amendments were technical or ministerial, forcing the court to determine the materiality of the items included in the proposal. The court began its analysis by emphasizing the dual purposes of the Unbundling Rules as set forth by the SEC in the Adopting Release: (1) to allow shareholders to "communicate to the board of directors [shareholders'] views on each of the matters put to a vote" and (2) to not force shareholders "to approve or disapprove a package of items and thus approve matters they might not if presented independently."[61] In light of these dual purposes, the court reasoned that "management may not propose several, aggregated charter amendments 'by treating them as . . . [one] vote on the restatement of corporate documents,' but it may combine 'ministerial or technical matters' that do not alter substantive shareholder rights."[62] The court held that Apple's proxy grouping impermissibly forced shareholders to approve or disapprove a package of items they would not have approved or disapproved if the items had been presented independently and denied shareholders the ability to communicate to management their views on each item put to a vote.[63]

The court then discussed the materiality of each bundled item. Beginning with the elimination of the board's blank check authority, the

58. *Id*. at *6.

59. *Id.* at *15–16.

60. The first defense—that the proposal was limited to amending the corporate articles—was dismissed because there were four discrete proposals "that, unless ministerial or technical, require separate shareholder votes." *Id.* at *16. As to the second defense—that Apple's proxy statement was consistent with numerous other proxy statements—the court reasoned that none of the proxy statements cited by Apple had been held to comply with SEC rules, so this argument was "of no moment." *Id.* at *17. The court threw out the third defense—SEC inaction—declining to draw the inference that the proxy statement was in compliance simply because the SEC had failed to act. *Id.* at *17–19.

61. *Id.* at *14 (quoting Communications Among Securityholders, *supra* note 3, at 29,566).

62. *Id.* at *14–15 (quoting RANDALL S. THOMAS & CATHERINE T. DIXON, ARANOW & EINHORN ON PROXY CONTESTS FOR CORPORATE CONTROL § 9.01, at 9-23 to -24 (3d ed. 1999)).

63. *Id*. at *15.

court found that Apple's claim that it would seek shareholder approval before issuing preferred stock in the future was unsupported by the facts[64] and that "the very existence of th[e] action . . . suggests that elimination of the 'blank check' provision is indeed material."[65] Moreover, the court noted that the provisions relating to majority voting and to par value could be deemed material; thus, the court was not persuaded by Apple's assertion that shareholders could cast their ballots simply based on their preferences with respect to blank check authority.

In reaching its conclusion that the Unbundling Rules were violated, *Greenlight Capital* provides three important interpretative principles. First, the court stated that even if the additional items were merely technical, bundling numerous technical matters with a single *material* matter violated the Unbundling Rules.[66] Second, it recognized that some of the proxy advisory services (namely, ISS and Glass Lewis) had noticed that the proposals were bundled together, and one of them (Glass Lewis) had also indicated that there were two material matters in Proposal Number 2, which the court considered to be additional evidence that Apple's proxy statement violated the Unbundling Rules.[67] As we discuss below, both of these concepts have broad applicability.

Finally, with respect to the fifth defense—that Proposal Number 2 was "pro-shareholder" and therefore not prohibited—the court noted that "coercive manipulation" of shareholder voting is only one "evil" addressed by the Unbundling Rules.[68] The court reasoned the Unbundling Rules can be violated without considering whether the joined proposals are pro- or anti-shareholder rights or value. We observe that the court's reasoning on this point is consistent with that employed by the Supreme Court in *Mills v.*

64. Apple's assertion was that the amendment removing the board's blank check authority was immaterial because the board would not issue preferred stock in the future without shareholder approval. Apple's board thus argued, albeit unsuccessfully, that as a practical matter the blank stock authorization was superfluous. However, the court pointed out that if the proposal was not approved the board would still have the power to issue preferred stock without shareholder approval, even if it chose not to exercise that power immediately. *Id.* at *19–20.

65. *Id.* at *20. This assertion was supported by a reference in Greenlight's reply brief which stated "[t]hat Apple, its shareholders, and entities like Egan Jones and ISS are debating this issue is a hallmark of materiality." Reply Memorandum of Law in Support of the Greenlight Entities' Motion for Preliminary Injunction at *3–4, Greenlight Capital v. Apple, Inc., 2013 U.S. Dist. LEXIS 12930 (S.D.N.Y. Feb. 15, 2013) (No. 13-cv-900-RJS).

66. *Greenlight Capital*, 2013 U.S. Dist. LEXIS 24716, at *21–22 ("Permitting Apple to bundle numerous 'technical' matters with a single material matter would appear to still violate the letter of the law . . . .").

67. *Id.* at *21.

68. *Id*. at *22.

Electric Auto-Lite Co. where the Supreme Court held that the Seventh Circuit committed reversible error by using the fairness of the merger terms to serve as a surrogate for whether a material omission was causally related to the effectuation of a merger.[69] Consistent with *Mills*, *Greenlight Capital* reasoned that the Unbundling Rules are not guided solely by whether bundling presents shareholders a distorted choice. Rather *Greenlight Capital* held that the Unbundling Rules are also directed at facilitating the goal of permitting shareholders to communicate their views to the board of directors on each matter put to a vote, and that purpose was defeated by bundling the proposals together. Thus, the rules are not solely directed toward proposals that are intentionally coercive in management's view because what is and what is not "pro-shareholder" is for the shareholders to decide.

B. SEC RESPONSES TO *KOPPEL* AND *GREENLIGHT CAPITAL*

In recent years, in response to *Koppel* and *Greenlight Capital*, the SEC has provided some additional guidance on the scope of the Unbundling Rules. As we will see, the SEC's approach diverges from that taken by the courts.

1. The SEC's 2004 Guidance & the 2015 Compliance and Disclosure Interpretation

In 2004, the SEC set forth guidance ("2004 Guidance") about the scope of the Unbundling Rules in the M&A context. In this release, the SEC focused on bundling concerns raised by practitioners posed by corporate governance-related or control-related provisions in the context of mergers and other acquisitions where, in connection with the transaction, shareholders of the surviving firm undergo a change in their rights or the firm's organic structure.[70] The SEC stated that when charter, bylaw, or similar provisions will become applicable as a result of an acquisition transaction, unless they are immaterial, the provisions should be presented as separate voting proposals whenever "the provisions in question were not previously part of the company's charter or bylaws[,] the provisions in question were not previously part of the charter or bylaws of a public acquiring company[,] and state law, securities exchange listing standards, or the company's charter or by-laws would require shareholder approval of

69. *See* Mills v. Elec. Auto-Lite Co., 396 U.S. 375, 381–83 (1970).

70. U.S. Sec. Exch. Comm'n, Div. of Corp. Fin., *Manual of Publicly Available Telephone Interpretations*, U.S. SEC. EXCH. COMM'N, https://www.sec.gov/interps/ telephone/phonesupplement5.htm (last modified Sept. 20, 2004).

the proposed changes if they were presented on their own."[71] The particular examples it provided that it believed required separate votes were for "classified or staggered board[s], limitations on the removal of directors, supermajority voting provisions, delaying the annual meeting for more than a year, elimination of ability to act by written consent, and/or changes in minimum quorum requirements."[72] Each of the preceding, the SEC reasoned, must be subject to a single vote.

It is not possible to say the SEC's 2004 Guidance dampened the appetite for bundling in connection with acquisition transactions.[73] Indeed, Lucian Bebchuk and Ehud Kamar reach a conclusion similar to our findings below: their study of mergers and acquisitions finds that impermissible bundling occurs frequently in mergers and acquisitions.[74] They focus on mergers that bundle in a staggered-board structure into the surviving corporation.[75] Despite serious investor opposition to staggered-board structures, they show that in a significant number of mergers, moves to staggered-board structures were indirectly approved by shareholders as a component of their vote approving the merger.[76] Bebchuk and Kamar argue that the "evidence suggests that control of the corporate agenda enables management to win approval of measures that shareholders would not approve on a stand-alone basis."[77]

71. *Id.* However, bylaws that are permitted by the company's governing documents to be amended by the board of directors are not required to be unbundled.

72. *Id.*

73. The 2004 Guidance also offered examples of circumstances in which unbundling would not be required. First, where an acquired company will be merging into a public company, unbundling is not required in certain circumstances; where the acquiring public company has provisions in its charter that differ from those of the acquired company, and the provisions of the acquirer's charter are not changing in connection with the merger, unbundling is not required. *Id*. This exception avoids "the unnecessary re-approval or ratification of a public company's pre-existing charter or bylaw provisions." *Id.* Also, where a target company has the same or similar provisions in its charter as those of the acquirer, no unbundling is necessary. *Id.* Further, shareholder rights plans "adopted in connection with a merger . . . generally would not be required to be unbundled" because shareholder approval is not generally required for a rights plan. *Id*. Finally, where shareholders of a target company will receive only cash consideration, unbundling is not required so long as their rights will not be affected by any provision which later takes effect. *Id*.

74. Bebchuk & Kamar, *supra* note 34, at 1567.

75. *Id*. at 1552.

76. *Id*. at 1552–53.

77. *Id.* at 1554. Bebchuk and Kamar examine three different types of mergers: continuing entity mergers (where A merges into B and B operates as the combined entity), new entity mergers (where A and B combine to form a new entity, C), and hybrid mergers (where A merges into B conditional on the approval of amendments in B's charter). *Id*. at 1563–65. They "show that the mergers . . . exhibit a strong tendency to be bundled with the introduction of a charter-based staggered board," but most prominently where the charter of the combined entity was new or an amended charter of one of the constituent firms because managers engage in opportunistic bundling when not confined to the existing

Addressing concerns regarding bundling in the M&A context, the SEC recently issued a new Compliance and Disclosure Interpretation ("2015 Interpretation").[78] The 2015 Interpretation, which supersedes the 2004 Guidance, provides more precise standards on whether M&A participants must unbundle proposals in merger and acquisition transactions.[79] Of significance to the subject of bundling examined here is that the SEC reiterates its prior position that "only material matters must be unbundled" and defines materiality in this context to mean a resolution that "substantively affect shareholder rights."[80]

2. The SEC's 2014 Compliance and Disclosure Interpretation

In 2014, partly in response to *Greenlight Capital*, the SEC released a Compliance and Disclosure Interpretation ("2014 Interpretation") on

charters of one constituent firm. *See id.* at 1567.

As demonstrated in the recent wave of tax inversion deals, the concern that companies bundle changes to governance provisions with votes on merger transactions remains relevant. For example, U.S.-based Alkermes, Inc. transitioned from annual director elections to a staggered board after its merger with a division of Ireland-based Elan Corporation. As in the Bebchuk and Kamar study, the staggered board was introduced in the proposal to approve the merger agreement rather than as a separate proposal, requiring shareholders to approve the staggered board if they voted to approve the merger. Alkermes, Inc., Preliminary Proxy Statement (Schedule 14A) 152–54 (June 23, 2011), https://www.sec.gov/Archives/edgar/data/874663/000095012311061225/y87033pmprem14a.htm. This experience, although outside the cluster of proxy proposals that define our data set, nonetheless raises concern that the problems identified by Bebchuk and Kamar persist. Our data set suggests that the urge to bundle, and regrettably the freedom to do so, is pervasive.

78. U.S. Sec. Exch. Comm'n, Div. of Corp. Fin., *Compliance and Disclosure Interpretations: Exchange Act Rule 14a-4(a)(3)*, U.S. SEC. EXCH. COMM'N, https://www.sec.gov/divisions/corpfin/guidance/exchange-act-rule-14a-4a3.htm (last updated Oct. 27, 2015) [hereinafter 2015 Interpretation].

79. The effect of the 2015 Interpretation remains to be seen. However, although the new 2015 Interpretation will require unbundling in some contexts where bundling was previously permissible, it is unclear whether the 2015 Interpretation will actually reduce the frequency of bundling or will merely provide practitioners with greater guidance on whether bundling is permissible (and how to structure M&A transactions so as to reduce the risk of a bundling violation). In a recent summary of the 2015 Interpretation, one practitioner noted that the Interpretation does "not introduce any significant new hurdles to obtaining shareholder approval in M&A deals. . . . For practitioners, this will make it easier to structure transactions where the need for an unbundled proposal can be factored in at the outset." Nicholas O'Keefe, *SEC Guidance on Unbundling in M&A Context*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Dec. 30, 2015), http://corpgov.law.harvard.edu/2015/12/30/sec-guidance-on-unbundling-in-ma-context/.

80. 2015 Interpretation, *supra* note 78. Pursuant to this standard, the shareholders' approval of a merger is not to be bundled with a material change in the acquiring firm's articles of incorporation or bylaws. Thus, if the plan of merger calls for the acquiring firm to adopt a classified or staggered board of directors, the SEC concludes this would be a material impact and both the stockholders of the acquirer and acquired firm should have a separate vote on the amendment. *See id.* The same result holds if the acquisition takes the form of a consolidation whereby the constituent corporations merge into a newly created entity whose governance structure introduces a material change. *Id*.

bundling of voting items outside of the M&A context.[81] The 2014 Interpretation discusses whether the Unbundling Rules are violated in three distinct situations. We closely examine each situation to ascertain whether the SEC's current views are consistent with the preceding judicial and administrative interpretations.

In the first scenario, corporate management proposed coupling in a single resolution a reduced dividend on its preferred stock and an extension of the maturity date. The 2014 Interpretation reasons that both items—the reduction in dividend and extension of maturity—could be included in a single vote because "multiple matters that are so 'inextricably intertwined' as to effectively constitute a single matter need not be unbundled."[82] Since both provisions related to "basic financial term[s] of the same series of capital stock and [each] was the sole consideration for the countervailing provision," the SEC viewed the two items as inextricably intertwined and therefore in need of only a single shareholder vote.[83]

Even though we agree with the result reached in the first situation analyzed in the 2014 Interpretation, we are concerned that the SEC did not choose to cabin its guidance to stock reclassifications and instead rested solely on a new standard—"inextricably intertwined"—that is ambiguous. "Inextricable" is defined as that "from which one cannot extricate oneself" or that which is "incapable of being disentangled, undone, or loosed."[84] Because the rights, privileges, and preferences enjoyed by a class of stock could, as a theoretical matter, always be serially amended, the use in the 2014 Interpretation of "inextricably" must have meant change, as a practical matter, whereby the voting stockholders could not reap the advantage of receiving dividends for a longer term unless the stockholders also accepted a lower dividend. Even this perspective, however, does not redeem the ambiguity because the proxy rules expressly permit the board to condition effectiveness of any approved matter (for example, a longer duration of the outstanding preferred shares) on the shareholders' approval of another matter (for example, the reduced dividend).

Our concern with the generality of the 2014 Interpretation on this matter is heightened by questioning what the SEC's position would be today if confronted with the 1980s' midstream recapitalizations, discussed

81. U.S. Sec. Exch. Comm'n, Div. of Corp. Fin., *Compliance and Disclosure Interpretations: Exchange Act Rule 14a-4(a)(3)*, U.S. SEC. EXCH. COMM'N, https://www.sec.gov/divisions/corpfin/guidance/14a-interps.htm (last updated Jan. 24, 2014) [hereinafter 2014 Interpretation].

82. *Id.*

83. *Id*.

84. *Inextricable*, THE RANDOM HOUSE COLLEGE DICTIONARY (rev. ed. 1988).

earlier, that prompted the adoption of the Unbundling Rules. It would have been easy to claim that one-time dividend payouts and the issuance of dual class voting stock are "inextricably intertwined," and therefore that only one vote is required. But this result is inconsistent with the forces that prompted the SEC to adopt the Unbundling Rules, namely the bundling practices in connection with the dual class recapitalization abuses of the 1980s. Furthermore, it seems inevitable to us that practitioners will claim many proposals are inextricably intertwined no matter how tenuous the connections between them. Given that the 1992 rules were adopted in order to avoid the difficulties in determining whether matters were "related," the SEC should not recreate the same type of ambiguity.

A less pernicious approach, and one consistent with the core philosophy of the Unbundling Rules, is to view the first situation covered by the 2014 Interpretation narrowly as a "recapitalization" that involves alteration of existing rights embedded in the preferred shares contract. Such transactions are legally the same as an exchange transaction in which an existing bundle of rights, privileges, and preferences enjoyed by a class of stockholders is swapped for a different bundle of rights, privileges, and preferences. Moreover, no other class of shares is similarly affected as the change is isolated to that section of the articles of incorporation wherein the affected preferred stock contract is defined. This perspective allows the transaction to be seen as a single matter: the exchange.

The unwieldiness of the unqualified "inextricably intertwined" standard is illustrated by litigation involving Groupon, where management sought to increase total authorized shares *and* to increase the total allowable allotment to individuals. Because Groupon did separate the proposals, the Groupon shareholders were able to approve the former, but not the latter.[85] The approach here shows the benefit of allowing shareholders to express their position on each of the substantive components of management's initiative. Under the 2014 Interpretation, however, management would have been allowed to bundle in a single proposal an increase in the total authorized shares with a proposal to increase individual allotments to managers. This part of the 2014 Interpretation's "inextricably intertwined" litmus not only confuses this area of law, but effectively curtails shareholders' right to vote separately on each item when the items relate to the same plan of action because management would generally prefer to bundle the items in a single vote. This is avoided if the first situation examined in the 2014 Interpretation is

85. Complaint, *supra* note 53, at 5–6.

isolated to instances of share recapitalizations so that the transaction is understood as an exchange between the corporation and a particular class of shares whereby a suite of rights, privileges, and preferences are exchanged for a different bundle of rights, privileges, and preferences.

In the SEC's second fact pattern, the SEC hypothesizes an instance where management seeks to amend the corporate charter to establish a par value for common stock, to eliminate provisions of a series of stock no longer outstanding that is not subject to further issuance, and to declassify the board of directors. According to the 2014 Interpretation, no violation is present because "[t]he staff would not ordinarily object to the bundling of any number of immaterial matters with a single material matter."[86] This statement implies that only proposals with at least two material matters would violate the Unbundling Rules—a conclusion that flies in the face of the court's opinion in *Greenlight Capital* which stated exactly the opposite standard. An additional concern is whether this norm can be administered effectively given the difficulty, discussed later, in resolving when a proposal is material. Finally, this new SEC standard will require courts and shareholders to carefully examine every item within a potentially long list of bundled proposals to determine its materiality. This will be time consuming and generate unnecessary costs.

In the final fact pattern discussed in the 2014 Interpretation, management seeks to change four aspects of an executive compensation scheme, including increasing the number of shares available as compensation, adding restricted stock to the compensation packages, and extending the term of the plan. The SEC stated that these four proposals can be bundled: "[T]he staff will not object to the presentation of multiple changes to an equity incentive plan in a single proposal . . . . This is the case even if the changes can be characterized as material . . . ."[87] Note that this part of the 2014 Interpretation does not require that these proposals be "inextricably intertwined." Rather, it effectively creates a significant carve-out from the Unbundling Rules for equity compensation plans. We find it odd that the SEC would make such a decision without seeking input from shareholders about the merits of such a carve-out: we question what is so special about executive compensation voting that it should be exempted from the Unbundling Rules?

An additional area where the 2014 Interpretation falls short is the SEC's discussion of *why* a firm might want to engage in bundling. The

86. *See* 2014 Interpretation, *supra* note 81.
87. *Id.*

SEC does not consider that the costs saved by combining items, rather than presenting the items separately, are at most *de minimis*, as the firm is already engaged in a proxy solicitation in the first place and will not have to spend any more effort describing the proposals when they are presented separately than when they are combined. In other words, the SEC does not isolate or attempt to analyze the practical benefits of combining items. In contrast, we believe it fairly apparent what the consequences are for management and the shareholders of bundling. Simply stated, bundling may be used by management to distort shareholder choice as well as to deprive shareholders of the opportunity to communicate their views on each proposed change. Hence, to recognize and encourage bundling more widely, as the 2014 Interpretation effectively does, seems contrary to the Unbundling Rules' foundation in fundamental notions of fair shareholder voting without providing any clear benefit. This controversial position is all the more problematic when reached without considering the nominal burdens of unbundling.

In all, the SEC's recent guidance does little more than muddy the waters, obscuring the line between what must be unbundled and what must not. The SEC itself appears to be aware that its recent guidance has not resolved the confusion over bundling—indeed, its efforts to unbundle resolutions has increased over the past few years: whereas the SEC only issued twenty-seven comment letters referencing bundling in 2011 and 2012, that number increased to seventy-one in 2013 and 2014.[88]

In sum, recent actions by the SEC in this area, such as the 2014 and 2015 Interpretations, and an increase in bundling-related comment letters, suggest that the SEC is taking an increased interest in impermissible bundling. Nonetheless, the SEC's attempts have thus far been unsuccessful—the recent guidance has been unclear and has further muddied the water in this important area. Further, its recent guidance provides ample opportunity for managers to bundle management-

88. Jim Moloney, Cem Surmeli & Erin Cho, *Unbundling Proposals After the Holidays*, DEAL LAW., Jan.–Feb. 2016, at 6–7. For an example of an SEC comment letter referencing impermissible bundling, see Letter from Kristina Arberg, Sec. Exch. Comm'n, to Christoper J. Vohs, Chief Accounting Officer, Bluerock Residential Growth REIT, Inc. (Dec. 23, 2013), https://www.sec.gov/Archives/edgar/data/1442626/000000000013069990/filename1.pdf ("We note that proposal number 1 is seeking shareholder approval to make multiple amendments to the charter, including, but not limited to, adding two new classes of common stock with different rights. Please revise your proxy statement to unbundle the proposed amendments into separate proposals as appropriate."). Although such comment letters can help to minimize bundling, we note many obvious examples of bundling did not receive SEC comment letters. For example, none of the bundling examples provided in Part III received SEC comment letters referencing the bundled proposals.

entrenching amendments on the backs of items more likely to receive shareholder approval.

C. PROXY ADVISORS AND BUNDLING

Another place where we might find a careful analysis of the Unbundling Rules is in the voting policies of third party voting advisors, such as ISS and Glass Lewis. Proxy advisors analyze all of the management proposals and provide voting recommendations to their institutional investor clients. Consequently, their voting policies have an important effect on shareholder votes.[89] In *Greenlight Capital*, the court recognized that proxy advisors had issued voting recommendations on the contested proposals. One of those voting services had found that "[Apple] has elected to bundle multiple article amendments into a single proposal, a practice which we believe negatively affects shareholders as it prevents them from judging each amendment on its own merits."[90] The fact that these voting advisors believed that these proposals were being bundled appears to have influenced the court's decision against Apple.

Because of the central role that proxy advisors play in the shareholder voting process, we examine the policies with respect to bundling of the two dominant advisors, ISS and Glass Lewis. While sometimes criticizing the bundling of management proposals in its reports,[91] ISS does not have a policy to recommend against a management proposal just because of its bundled nature.[92] Instead, their 2015 proxy voting guidelines state:

> Vote case-by-case on bundled or 'conditional' proxy proposals. In the case of items that are conditioned upon each other, examine the benefits and costs of the packaged items. In instances when the joint effect of the conditioned items is not in shareholders' best interests, vote against the proposals. If the combined effect is positive, support such proposals.[93]

89. James Cotter, Alan Palmiter & Randall Thomas, *ISS Recommendations and Mutual Fund Voting on Proxy Proposals*, 55 VILL. L. REV. 1, 6–8 (2010).

90. Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716, at *24 (S.D.N.Y. Feb. 22, 2013).

91. For example, ISS notes in one report that "[b]undled proposals can leave shareholders with an all-or-nothing choice, skewing power disproportionately towards the board and away from shareholders." INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING FIRSTMERIT CORP. 11 (Apr. 3, 2007). Similarly, ISS notes in another report that "[i]t is best corporate governance practice that the company submit key amendments independent of one another and not bundle multiple amendments into one item" INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING HOLLY CORP. 8 (June 14, 2011) [hereinafter HOLLY CORP.].

92. In fact, as discussed in Part III, ISS reports rarely explicitly highlight the bundled nature of the proposal.

93. INST'L S'HOLDER SERVS. (USA), SUMMARY PROXY VOTING GUIDELINES: 2015

In sum, ISS's policies state that it will recommend "for" the bundled proposal if the net effect of the different items is perceived as beneficial to shareholders and "against" if the net effect is perceived as detrimental to shareholders.

In practice, however, ISS's actual recommendations do not always match its stated policy, perhaps highlighting the challenge of consistently implementing such a policy. We find that ISS sometimes recommends "against" if any of the bundled items would get an "against" recommendation on a stand-alone basis. This implies a negative recommendation if there is a "bad" item in the bundle, no matter how many other items are "good." For example, in the ISS report on Holly Corporation's management proposals in 2011, ISS states: "In analyzing bundled proposals, ISS will recommend AGAINST a proposal if any one of the bundled issues is not in the best interests of shareholders."[94] Either way, both the ISS stated policy and its application seem inconsistent with the judicial decisions and SEC interpretations discussed above; the courts and even the 2014 Interpretation deem bundling unlawful when two or more material items are joined, regardless of their perceived impact on shareholder rights. We believe the proxy advisors' practice of assessing whether the bundled material matters yield a net benefit has the same shaky wisdom as being a little bit misleading in one's material statements.

As for Glass Lewis, we did not find any mention of bundling in the Glass Lewis 2011[95] and 2013[96] Proxy Paper Guidelines, suggesting that Glass Lewis may not have had an explicit policy on bundling. In the 2015 guidelines, we found the following:

- If a board seeks shareholder approval of a forum selection clause as

BENCHMARK POLICY RECOMMENDATIONS 32 (updated Mar. 4, 2015), http://www.issgovernance.com/file/policy/2015-us-summary-voting-guidelines-updated.pdf. The same language has been repeated in the Summary Proxy Voting Guidelines every year since 2003, the first year for which we have ISS guidelines. The only other mention of bundling in the ISS 2015 proxy voting guidelines is in the context of anti-greenmail proposals and essentially is just an example of this general policy: "Vote case-by-case on anti-greenmail proposals when they are bundled with other charter or bylaw amendments." *Id.* at 24.

94. HOLLY CORP., *supra* note 91, at 8. *See also* INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING HAWAIIAN ELECTRIC INDUSTRIES, INC. 15 (Apr. 16, 2009) ("[ISS's] policy regarding bundled proposals is to support the entire bundled proposal only if [ISS] would support each individual part of the bundled proposal on a standalone basis."); INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING INTERSIL CORP. 15–16 (May 11, 2005) ("ISS will analyze the following proposal as a bundled proposal. If one of the items brought to vote under the amendment receives an against vote recommendation, then we will recommend an against vote regarding the entire proposal.").

95. GLASS LEWIS & CO., LLC (USA), PROXY PAPER GUIDELINES: 2011 PROXY SEASON: AN OVERVIEW OF THE GLASS LEWIS APPROACH TO INTERNATIONAL PROXY ADVICE (2011).

96. GLASS LEWIS & CO., LLC (USA), PROXY PAPER GUIDELINES: 2013 PROXY SEASON: AN OVERVIEW OF THE GLASS LEWIS APPROACH TO PROXY ADVICE (2012).

part of a bundled proposal rather than as a separate proposal, Glass Lewis will "weigh the importance of the other bundled provisions when determining the vote recommendation on the proposal."[97]

- Glass Lewis will recommend against the chairman of the governance committee if the board is currently seeking shareholder approval of a forum selection clause as part of a bundled proposal rather than as a separate proposal.[98]

Based on the above, it seems that Glass Lewis does not have a general policy on bundling, and even these specific applications were introduced into its guidelines only recently.

If we can extrapolate from the exclusive forum case shown above, it appears that Glass Lewis's general policy is to assess the overall net effect of bundled proposals; this mirrors ISS's approach. As we noted with ISS, this is not consistent with the judicial and SEC authority discussed above. Because of the similarity in the ISS and Glass Lewis policies, in the empirical analysis in Part V, the cases of bundling where Glass Lewis and ISS recommendations differ will be examples of how the two proxy advisors made that "net effect" assessment differently, further highlighting the difficulty in administering this policy consistently.

In our eyes, the third party voting advisors should have clear policies against bundling violations that comply with the courts' decisions in *Koppel* and *Greenlight Capital*. If they find that a proposal is improperly bundled, then they should automatically issue a negative voting recommendation. We believe this approach would have the salutary effect of both highlighting the existence of bundling and reducing its incidence. Proxy advisors' current standards and their application not only muddy the waters, but may well encourage bundling when managers believe the coupled proposals can be seen as yielding a net benefit. And their inherent ambiguity introduces costs and uncertainty into their operations, which does not benefit their clientele and likely raises their operating costs.

Proxy advisors, by basing their decision on whether bundled material items yield a "net benefit" are guiding their recommendations by a maxim "no harm, no foul." Whatever reasoning supports the maxim, it is not appropriate in this context. The proxy advisors' net benefit approach is at

97. GLASS LEWIS & CO., LLC (USA), PROXY PAPER GUIDELINES: 2015 PROXY SEASON: AN OVERVIEW OF THE GLASS LEWIS APPROACH TO PROXY ADVICE 39 (2015), http://www.glasslewis.com/assets/uploads/2013/12/2015_GUIDELINES_United_States.pdf.

98. *Id.* at 14.

odds with *Mills v. Electric Auto-Lite Co.*, where, as seen earlier, the Supreme Court held a material omission violates the proxy rules *regardles*s of the fairness of the particular transaction the shareholders are asked to approve.[99] We believe the proxy advisors' net benefit approach to bundling is even more invidious than the case posed in *Mills* because their practice essentially licenses managers to remove the shareholder vote on any separate matter needing their approval so long as managers deftly join that matter with a higher-valued matter. Clearly a "foul" exists here as well as a proscribed harm.

While drawing the line between bundled and unbundled proposals is occasionally difficult, the vast number of instances of bundling are easily detected. Moreover, proxy advisors are the most experienced shareholder representatives in spotting bundling issues. As we show in the next sections, most improperly bundled proposals can be (and are) uncovered by applying several basic rules.

III. DISTINGUISHING AMONG BUNDLES OF BUNDLING

Having reviewed the main authoritative sources interpreting the Unbundling Rules, we now describe four different criteria to identify bundled management proposals. As will be seen, our criteria for each of the four analytical groups are shaped by the distinct public policy implications posed by each of the forms that bundling can take. We consider the following potential definitions of bundling: "generic bundling," "material bundling," "multiple material bundling," and "negative bundling." As a prelude, we point out that our four groups are ordered here so that the most inclusive group, generic bundling, appears first, and as we move to other categories the bundling criteria tightens so that fewer instances are reported.[100]

A. GENERIC BUNDLING

We define as "generic bundling" cases where multiple proposals are aggregated on the proxy card so that a shareholder casts but a single vote

99. Mills v. Elec. Auto-Lite Co., 396 U.S. 375, 381–83 (1970).

100. To elaborate, generic bundling appears first because it includes all bundling observations falling within the next three categories plus any non-material bundled proposals. Material bundling collects all the instances of single and multiple material proposals that are bundled, including negative bundling, but excludes non-material bundled items that would be included only within the general bundling rubric. Similarly, multiple material bundling is less inclusive than material bundling, as the material bundling category collects both single and multiple bundled proposals. Finally, the least inclusive category is negative bundling, which includes only those resolutions within material or multiple material bundling in which at least one proposal negatively impacts shareholders.

for all the proposals (regardless of whether the individual items are viewed as material and regardless of whether their perceived effect on shareholders is positive or negative). Hence, this is the broadest definition of bundling, and this type of bundling is also the easiest standard to apply for empirical research (or for that matter enforcement) as it only requires us to count whether more than one proposal is to be acted upon through a single shareholder vote.

Generic bundling does not necessarily violate the Unbundling Rules. As noted earlier in the discussion of *Greenlight Capital*, bundling together "'ministerial or technical matters' that do not alter substantive shareholder rights" is generally permitted.[101] Nonetheless, both *Koppel* and *Greenlight Capital*, relying on the Adopting Release, not only interpret the Unbundling Rules to require that "separate matters" be put to separate votes, but in doing so expressed a strong preference for more voting items rather than fewer.[102] What constitutes a separate item is a matter for state law, or absent such law, is a question of fact to be determined from the underlying corporate documents.[103] Hence, it is important to examine the frequency with which generic bundling occurs. Such frequency defines the universe of potential bundling violations because in principle each item in the bundled proposal could be a "separate matter."

We raise here the view that generic bundling of items that are admittedly technical and ministerial is not beyond concern. As we move through the next three analytical categories of bundling, we parse generic bundling further as we explore whether managers systematically exploit the law's ambiguities. The frequency with which we find generic bundling piques this inquiry, as does the fact that each item in the bundled proposal could be a "separate matter." That is, if items of any significance could be easily separated so that the shareholders are thereby empowered to vote effectively on each item so separated, why do we find the opposite—pervasive clustering of seemingly unrelated items? To resolve this question, we separately analyze the materiality of each proposal grouped

101. Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716, at *15 (S.D.N.Y. Feb. 22, 2013) (quoting THOMAS & DIXON, *supra* note 62, at 9-23, 9-24). Proposal 3 from Loews Corporation's 2009 meeting is an example of a bundled proposal including only technical or ministerial items. Loews Corp., Definitive Proxy Statement (DEF 14A), at 23–24 (Apr. 7, 2009), http://www.sec.gov/Archives/edgar/data/60086/000006008609000013/proxy2009final.htm. This proposal requested permission to simplify and update the charter by revising the purpose clause and eliminating unnecessary provisions relating to outdated stock.

102. *See* Koppel v. 4987 Corp., 167 F.3d 125, 138 (2d Cir. 1999); Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716, at *13–14 (S.D.N.Y. Feb. 22, 2013).

103. *Id.*

with others in the same resolution as well as the substantive impact on shareholders of each material proposal that is bundled. With these further refinements, described below, a sharper image of the frequency and perniciousness of bundling is presented.

B. MATERIAL BUNDLING

A higher threshold than generic bundling for a violation of the Unbundling Rules requires that the management proposal include at least one material item bundled with other technical or material items. To operationalize this threshold, we define as "material bundling" the subset of generic bundling where at least one of the items in the bundled proposal is material.

One challenge with this definition of bundling is that it requires a decision maker to determine if a particular management resolution contains at least one material proposal. In our empirical analysis, to assess whether a certain proposal would materially affect shareholder rights, we rely on the current view of best practices in corporate governance as reflected in various corporate governance ratings, proxy voting advisor recommendations, and voting policies of major institutional investors,[104] such as the Council for Institutional Investors. Moreover, in *Greenlight Capital*, the court interpreted the fact that proxy advisory services had themselves noted that two material proposals were bundled together to be further evidence that those proposals were bundled.[105] Hence, to aid in our materiality assessment, when available, we also read proxy advisors' analysis of the items contained in the bundled proposals.

As an example of this type of bundling, consider the 2005 annual meeting of MKS Instruments, Inc., which asked shareholders to cast a single up-or-down vote on a single group that contained six bylaw amendments, claiming that the amendments were "primarily to reflect" various changes to Massachusetts corporate law.[106] While some of these

104. We note that our resort to objective evidence in the form of best practices is consistent with the materiality standard customarily invoked in regulatory and enforcement matters. *See, e.g.*, TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976) ("A[] . . . fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote . . . . It does not require proof of a substantial likelihood that disclosure of the . . . fact would have caused the reasonable investor to change his vote."). A proposal of the type fitting within such documented best practices is a matter that typically causes at least pause on the reasonable shareholder's part before casting a vote on that matter.

105. *Greenlight Capital*, 2013 U.S. Dist. LEXIS 24716, at *21.

106. INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING MKS INSTRUMENTS, INC. 8–9 (2005).

amendments did in fact reflect such changes (and may be viewed as technical items), at least one proposed bylaw amendment—to permit directors unilaterally to amend provisions relating to the removal of directors without shareholder approval—would result in a material (and arguably adverse) change to shareholders' rights that did not appear required by the statutory change. ISS highlighted "the bundled nature of this proposal" and recommended against its approval because of this amendment.[107]

The MKS Instruments proxy is an example where (at least) one material item within a bundled proposal was accompanied by several other purportedly ministerial and technical amendments. This bundled resolution violated the standard set forth in *Greenlight Capital*, but not the 2014 Interpretation. But, perhaps more importantly, it also illustrates the significant difficulties facing shareholders under the standard set forth in the 2014 Interpretation proposal. In order to determine if the <u>six</u> bylaw amendments grouped within a single resolution were material, a shareholder (or their advisor) would need to: (1) carefully read each of the six amendments, (2) determine if—without reference to other bodies of law—any of the six changes was material, (3) consult an attorney to determine if any changes to Massachusetts or federal law made an otherwise material proposal merely technical or ministerial, and then (4) determine how many of the proposed changes materially affected shareholder rights. Only after completing all of these steps could an investor (or their voting advisor) determine if this single proposal violated the Unbundling Rules. Given the complexity of this process, and the inherent subjectivity of the inquiry entailed, it is likely that different shareholders and different proxy advisors would reach different conclusions.[108]

As discussed below, we recommend that companies be required at least to present each separate material proposal as a single voting item. That is, we recommend that our definition of "material bundling" be used as the standard for impermissible bundling (consistent with the standard set forth in *Greenlight Capital*).[109] Although our recommendation is inconsistent with the SEC's 2014 Interpretation, which rejects the approach

107. *Id.*

108. *See infra* Part IV for data on the differences in voting recommendations on bundled proposals among proxy advisors.

109. *Greenlight Capital*, 2013 U.S. Dist. LEXIS 24716, at *21–22 ("Permitting Apple to bundle numerous 'technical' matters with a *single* material matter would appear to still violate the letter of the law . . . ." (emphasis added)).

taken in *Greenlight Capital* by concluding that the joinder of a single material proposal with several ministerial and technical proposals does not violate the Unbundling Rules,[110] we believe the SEC's 2014 Interpretation is inconsistent with the animating objectives of the Unbundling Rules as well as in conflict with corporate law.

We believe such a standard is necessary because if companies are instead permitted to combine a material proposal and a constellation of other proposals as a single voting item, as condoned by the 2014 Interpretation, the rule becomes very difficult for the SEC to administer and for shareholders and proxy advisors to intelligently apply. By interpreting the Unbundling Rules to at least require each material proposal to be separately voted upon, the Unbundling Rules will be applied so as to avoid trivializing state corporate law provisions that compel shareholder approval of a matter even if that matter is recognized to be technical and ministerial.[111]

We in fact recommend that bundling concerns be broader than the court's position in *Greenlight Capital*. The court's conclusion that a single material proposal when joined with admittedly technical or ministerial items violated the Unbundling Rules implies that if only technical or ministerial proposals are combined there is no violation. One basis for believing this creates bad policy is that carving out an exception to the Unbundling Rules for the joinder of solely technical and ministerial proposals raises difficult and likely unmanageable interpretative problems in the SEC's oversight of the rule. Because thousands of proxy statements descend on the SEC, generally during the crowded two or three month "proxy season," concerns for the administrability of an interpretation is a desideratum. At a minimum, difficulty in ascertaining for a particular company whether the grouped proposals are all technical or ministerial supports a prophylaxis whereby a thumb is placed on the scale consistent with *Koppel*'s observation that over-inclusion is better than under-inclusion.[112] This approach is all the more compelling in light of the fact that separate presentation of proposals entail *no* marginal cost and, if for

110. 2014 Interpretation, *supra* note 81.

111. We believe that the SEC can adopt guidelines for enforcement of its Unbundling Rules so that, as a purely internal matter, the SEC can exercise prosecutorial discretion while at the same time continuing to administer its selective review of proxy statements in a manner consistent with our recommendations. In the end, its administration of the Unbundling Rules, similar to its position in the administration of the proxy rules overall, should be to facilitate governance by compelling separate presentation of even technical and ministerial proposals.

112. Koppel v. 4987 Corp., 167 F.2d 125, 138 (2d Cir. 1999) (citing Communications Release, *supra* note 3, at 48,287).

some reason there is the belief on management's part that approval of each proposal is necessary to achieve an important outcome, as seen earlier, the proxy rules expressly permit conditioning any approval on the approval of other separately voted on matters. Our call for a prophylactic response is further supported by our findings regarding not just the frequency of bundling of material items, but that clustered among bundled items are material items that are harmful to shareholders.

A further reason to disallow bundling of technical and ministerial proposals is that this type of bundling conflicts with the purposes underlying the Unbundling Rules as well as basic corporate law. As relied upon in *Greenlight Capital,* the Unbundling Rules' purpose was not solely to rid the proxy statement of distorted choices. As set forth in the Adopting Release, the Unbundling Rules facilitate shareholders' communication of their views on matters requiring their approval.[113] On this point, it is significant that the Unbundling Rules speak in terms of "separate items" as contrasted with the more ubiquitous material standard that customarily guides disclosures in SEC documents. The litmus used for the Unbundling Rules suggests an approach to the Rules' interpretation that is not less inclusive than whether shareholders would attach significance to the matter when deciding how to vote.[114] But there are considerations aside from the importance the proposal may assume to the reasonable shareholder.

Consider that, if the board is seeking shareholder approval of a matter that is indeed technical or ministerial, there must be some legal compulsion for the board to seek approval. The board cannot be expected to submit proposals to shareholders if the board has the legal authority to act without shareholder approval.[115] The board submits technical and ministerial proposals to the shareholder because the matter is in the charter and beyond the power of the board of directors to act alone to change.[116] Thus, as a matter of state law, corporate law does not quiet or ignore the voice of the

113. Communications Release, *supra* note 3, at 48,287.

114. *See supra* note 104 (discussing the standard of materiality).

115. An important qualification to this would be an instance where some element of self-interest drives the board to obtain the cleansing influence of the disinterested shareholder approval. *See* DEL. CODE ANN. tit. 8, § 144 (2016); MODEL BUS. CORP. ACT § 8.63 (AM. BAR ASS'N 2007).

116. The Model Business Corporation Act allows the board to act in very limited instances to remove some inconsequential items, for example, remove "Corporation" from its name, in the charter without shareholder approval. *See* MODEL BUS. CORP. ACT § 10.05. Because nearly half of all public companies are incorporated in Delaware, and thus the vast preponderance of the companies subject to the SEC proxy rules are Delaware companies, it is significant that the Delaware statute does *not* similarly authorize the board to undertake any change in the charter without stockholder approval after shares have been issued. *Compare* DEL. CODE ANN. tit. 8, § 241, *with id.* § 242.

shareholders on matters solely because management makes an ex ante determination that the item is technical or ministerial. We therefore believe it is inappropriate that *Greenlight* and the SEC permit the Unbundling Rules to be interpreted in a manner inconsistent with state corporate law. Our concern is even greater with the SEC's embrace of the view that matters management deems technical and ministerial can be presented for a single vote with a proposal acknowledged to be material in its own right. Certainly these positions are difficult to justify on the basis of cost when separate voting entails no marginal cost.

C. MULTIPLE MATERIAL BUNDLING

Our third classification of bundling arises where two or more material proposals are joined in a single resolution to be voted upon by the shareholders. Using the approach described in the preceding section, a proposal's materiality is determined in light of contemporary views of governance ratings, proxy advisors, and institutional investors. If there are two or more material proposals that are bundled, there seems to be no dispute that aggregating them into one single voting item will violate the Unbundling Rules.[117]

One example of what we define as multiple material bundling is Proposal Number 3 from the June 2005 annual shareholders' meeting of Majesco Entertainment. Majesco's management proposed, among other things, that its shareholders approve a restatement of its entire certificate of incorporation to add several strong antitakeover provisions.[118] These included: a classified board of directors, a prohibition on shareholder action by written consent, a limitation that directors could be removed only for cause, certain supermajority voting provisions, and a provision providing that the company would not opt out of the Delaware antitakeover statute.[119] ISS noted the tremendous antitakeover force of these changes and recommended that shareholders vote against the proposal (the "net effect" assessment was simple in this case because ISS viewed all the provisions as adversely affecting shareholder rights).[120] However, because management

117. Even Apple appears to have conceded this point in *Greenlight Capital*. *See* Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716, at *19 (S.D.N.Y. Feb. 22, 2013). The one exception to the rule would be the carve-out in the 2014 Interpretation for executive compensation plans. *See* 2014 Interpretation, *supra* note 81.

118. Majesco Entm't Co., Definitive Proxy Statement (DEF 14A), at 27–29 (May 9, 2005), https://www.sec.gov/Archives/edgar/data/1076682/000095013605002626/file001.htm.

119. *Id*.

120. INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING MAJESCO ENTERTAINMENT CO. 17–19 (2005).

(the Sutton family) controlled 36.3 percent of the company's voting stock,[121] it is not surprising that the proposal passed.[122]

Under the test in *Greenlight Capital*, this constitutes a blatant violation of the Unbundling Rules. In that case, the court held that "management may not propose several, aggregated charter amendments 'by treating them . . . as [one] vote on the restatement of corporate documents' . . . ."[123] This type of proposal shows why enforcing the Unbundling Rules is important.[124]

Another example is when, in 2008, ITT Corporation asked shareholders to approve an amendment to its certificate of incorporation that would simultaneously increase the number of its authorized shares of common stock by 100 percent and amend the company's bylaws to provide for majority voting for directors in uncontested elections.[125] These are material, but unrelated, matters; combining the two of them together in a single proposal violates the Unbundling Rules, as in the Majesco Entertainment example. Despite this impermissible bundling that presented a distorted choice, ISS did not recommend an "against" vote, explaining that the majority voting amendment was shareholder-friendly under the circumstances[126] and that the increase in authorized shares was "below the allowable threshold" for which ISS typically casts a skeptical eye.[127]

A special case of multiple material bundling—and one that most distorts shareholders' choice—occurs when one (or more) material proposal(s) that benefits shareholders is combined with one (or more) material proposal(s) that adversely affects shareholders. The dual class recapitalizations of the 1980s, discussed earlier, exhibited these characteristics. In a more recent time period, consider the example of Life Technologies Corporation. In April 2011, ISS published a report to its

121. Majesco Entm't Co., *supra* note 118, at 5.

122. Majesco Entm't Co., Current Report (Form 8-K) (June 13, 2005), https://www.sec.gov/Archives/edgar/data/1076682/000095013605003559/file001.htm.

123. Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716, at *14–15 (S.D.N.Y. Feb. 22, 2013) (quoting THOMAS & DIXON, *supra* note 62, at 9-23, 9-24).

124. This proposal is not an isolated occurrence of this type of behavior. For example, Schnitzer Steel Industries held a special meeting in 2006 to amend the company's charter to incorporate a host of antitakeover defenses and bundled all of the amendments into a single proposal. INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING SCHNITZER STEEL INDUS., INC. 5–6 (May 25, 2006).

125. INST'L S'HOLDER SERVS. (USA), PROXY REPORT TO ITT CORP. 13–14 (Apr. 21, 2008).

126. The report does not disclose whether shareholder approval of the bylaw amendment was necessary. *See id.* For example, if the directors had the power to amend the bylaws unilaterally, then including this item in the proposal was unnecessary and likely calculated to favorably influence the shareholder vote on the increase in authorized shares.

127. *Id.* at 14.

clients about Life Technologies Corporation's upcoming annual meeting at which there were several voting items on the ballot. Of particular interest for our purposes is Item 8 of the proxy statement, where corporate management sought in a single proposal to amend the company's certificate of incorporation to declassify its board of directors, adopt an exclusive venue provision for shareholder suits under Delaware law, and remove some provisions relating to a particular series of preferred stock.[128] Beginning with an item-by-item analysis, the ISS report first found that board declassification proposals would substantially increase board accountability to shareholders and hence should be supported by shareholders.[129] With respect to the exclusive venue provision, however, it recommended negative shareholder action unless the company had in place best practices in corporate governance, which Life Technologies did not at that time.[130] Finally, with respect to the preferred stock proposal, ISS felt it would have effectively led to the authorization of blank stock preferred stock, which the company could use for anti-takeover purposes; ISS viewed the proposed changes to the preferred shares negatively.[131]

Life Technologies' 2011 proxy statement appears to be a clear case where corporate management sought shareholder approval of three material items, two adversely affecting shareholder rights and one beneficial to shareholder rights, by bundling the three together with a single box on the ballot. Under any of the legal standards discussed above, this resolution in Life Technologies' proxy statement violated the Unbundling Rules. Nevertheless, in line with its stated policy on voting on bundled items, ISS recommended to shareholders that they vote in favor of this item. It stated, "given that these [preferred stock and exclusive venue] proposals are bundled with a declassification proposal that would substantially increase board accountability and give greater effect to the shareholder franchise, we recommend that shareholders vote FOR this bundled proposal."[132] It did qualify this statement by noting that in the future it might issue a negative voting recommendation if an issuer bundled an exclusive venue provision with any other proposal.[133]

When the ballots were counted, only 0.7 percent of shareholder votes

128. Life Technologies Corp., Definitive Proxy Statement (DEF 14A), at 47–50 (Mar. 18, 2011), https://www.sec.gov/Archives/edgar/data/1073431/000095012311026578/a58520dedef14a.htm.

129. INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING LIFE TECHNOLOGIES CORP. 11 (Apr. 11, 2012).

130. *Id*. at 10–11.

131. *Id*. at 10.

132. *Id.* at 11.

133. *Id*.

were against the proposal.[134] As developed in Part V, this outcome is consistent with the proposal receiving a positive ISS voting recommendation, despite its obvious violation of the Unbundling Rules. The clear implication of the ISS voting report is that ISS would not have recommended in favor of two of the three items bundled together if they had been presented to shareholders separately. This example clearly highlights the inconsistency between ISS voting recommendations and the Unbundling Rules as well as the destructive effect of bundling on shareholders' voices.

Cases of bundling combining a "positive" and a "negative" item, such as Life Technologies, are interesting because they capture the type of bundling that most distorts shareholders' choices by forcing shareholders to accept an item that they would not approve on a stand-alone basis in exchange for the approval of another item they favor. However, it is important to emphasize that it is not necessary that a single proposal aggregate material positive and negative items to violate the Unbundling Rules. Aside from the fact that shareholders may differ in their assessment of what is "positive" and "negative" (as *Greenlight Capital* indicates), and can likewise be expected to disagree as to the magnitude of any perceived negative or positive effect, the court in *Greenlight Capital* rejected Apple's claim that only intentional "coercive manipulation" through bundling by management is forbidden. There, the court noted that this form of manipulation of shareholder voting is only one "evil" addressed by the Unbundling Rules.[135] We emphasize that the Unbundling Rules are also directed toward permitting shareholders to communicate their views to the board of directors on each matter put to a vote, and that purpose is defeated by bundling material proposals together.[136] Hence, any management proposal with two or more material items contained in it—for example, any case we define as multiple material bundling—will violate the Unbundling Rules, regardless of whether those items are positive or negative.

D. NEGATIVE BUNDLING

Our fourth classification of bundling entails identifying instances in which multiple material proposals are bundled with at least one proposal

134. This data is derived from the ISS Voting Analytics Database. *Voting Analytics*, ISS, https://www.issgovernance.com/solutions/iss-analytics/voting-analytics/ (data set on file with authors).

135. Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716, at *22–23 (S.D.N.Y. Feb. 22, 2013).

136. *See supra* text accompanying note 38.

that negatively affects shareholders' rights.[137] In this classification we examine each material item and assess whether it results in an augmentation or diminution of shareholder rights.

Assessing the likely positive or negative effect of a material proposal is highly fact specific. In many instances, we could determine a proposal's positive or negative impact using the same third party sources previously employed to assess the materiality of the bundled items. Nonetheless, in making this assessment, we quickly discovered that the unique factual setting not only mattered, but mattered a good deal. For example, consider the facts in *Greenlight Capital*, where among the four proposals bundled was an amendment to the charter to eliminate the board's blank stock authority.[138] In some settings, and certainly before the advent of the poison pill defensive maneuver, a blank stock provision was touted as value-increasing as it enables the board to nimbly craft the terms of a preferred stock offering to meet the momentary expectations of investors who would be expected to purchase the preferred shares and thereby flush the corporation's treasury with cash. In the mid-1980s, this prince became a frog as boards regularly drew upon its blank stock authority to issue rights which were central to the poison pill defensive maneuver.[139] In the case of Apple, the blank stock provision was the means by which the activist shareholder, Greenlight Capital, sought to force the Apple board to distribute significant sums of cash that it believed Apple was needlessly hoarding. The distribution would have occurred through a special class of dividend preferred that the board could issue pursuant to its blank stock authority.[140] Thus, in this context, through a hedge fund's "kiss," the frog is restored to being a prince.

A further example of the idiosyncratic feature of positive and negative characterizations of a material proposal's effects is the ex ante effects of a super majority voting requirement. Many of the instances we observe of multiple material bundling involve changes in charter or bylaw provisions reducing a supermajority vote needed to amend the charter, to merge the firm, or to sell the firm. Such changes can be seen as positive, as a lower

137. In defining what is negative, we rely on the current view of best practices in corporate governance, as reflected in various corporate governance ratings, proxy voting advisor recommendations, and voting policies of major institutional investors, such as the Council for Institutional Investors.

138. *Greenlight Capital*, 2013 U.S. Dist. LEXIS 24716, at *4.

139. *See* Moran v. Household Int'l, Inc., 500 A.2d 1346, 1351–54 (Del. 1985) (describing the process and authority for creating poison pills via the board's blank stock authority).

140. *Greenlight Capital*, 2013 U.S. Dist. LEXIS 24716, at *5–6.

vote necessarily introduces a quality prized in commerce, greater flexibility and ease of accomplishing a transaction; a lower voting threshold to be acquired can also lead to the firm being acquired at an above-market price.[141] On the other hand, these positive effects are not present if the firm has a substantial block holder.[142]

Our point is not to argue that changes in supermajority voting requirements are inherently nefarious. Our point is more modest: it is difficult to assess the positive or negative effects of such a change, but not difficult to understand that each change is itself material.

One example of negative bundling is Proposal Number 2 from BB&T Corporation's 2004 annual meeting. The proposal sought to make the four following amendments to BB&T's bylaws: (1) declassify the board, (2) allow for removal of directors with or without cause, (3) enhance the ability of the board to fill vacancies, and (4) allow the board to amend the bylaws without a shareholder vote.[143] While the first two items increase shareholder rights, the third and fourth items restrict shareholder rights. In particular, the third item would have allowed a majority of the board to fill vacancies, including vacancies created because shareholders removed the director in question, while the fourth item would have allowed the board to bypass shareholders when making changes to the bylaws. This bundling incident also illustrates the difficulty proxy advisory services face in determining the overall net effect of a proposal. ISS ultimately decided to recommend against this proposal because "the potential negative impact of the proposed third and fourth amendments to the bylaws outweighs the benefits of an annual board and the increased accountability of directors."[144] However, Glass Lewis, which presumably also bases its recommendations on a proposal's net effect, recommended that

141. *See, e.g.*, Audra Boone, Brian Broughman & Antonio J. Macias, *The Cost of Supermajority Target Shareholder Approval: Mergers Versus Tender Offers* (Ind. Legal Studies Research Paper No. 331, 2016), http://ssrn.com/abstract=2629424 (finding statistically significant evidence that supermajority voting requirements impact the form of acquisitions).

142. For example, a pre-existing 20 percent owner whose ability to amend the charter or to merge or sell the firm is greatly facilitated by the concomitant lowering of the number of shares the block holder must persuade to its cause.

143. BB&T Corp., Definitive Proxy Statement (DEF 14A), at 7–10 (Mar. 24, 2004), https://www.sec.gov/Archives/edgar/data/92230/000119312504044964/ddef14a.htm#toc14357_4. Note that Majesco Entertainment, Life Technologies, and, arguably, ITT Corporation (depending on how one views the proposal to increase the number of authorized shares of common stock) are also examples of negative bundling in that in each of these cases at least one item in the bundle was material and adversely affected shareholder rights. *See supra* notes 118–129 and accompanying text.

144. INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING BB&T CORP. 14 (undated).

shareholders vote in favor of the proposal.[145]

The idea behind this category is that proposals that negatively affect shareholder rights are more likely to constitute abusive bundling instances and should therefore be viewed as more egregious violations of the Unbundling Rules. That is, including a proposal with distinctly negative effects on shareholder rights with material proposals that have positive effects entails the classic distorted choice that catapulted initial interest in the Unbundling Rules. The Unbundling Rules and their construction has moved past this narrow, albeit most harmful, type of bundling. It is important to reiterate that, for purposes of the Unbundling Rules, it does not matter whether the bundled proposals are individually positive or negative, or if their joinder overall yields positive or negative effects. *Greenlight Capital* holds that the rules are not solely directed toward proposals that are intentionally coercive in management's view because what is and what is not "pro-shareholder" is for the shareholders to decide.[146] Even a proposal that is labeled positive by some shareholders may not be positive from the perspective of other shareholders, so that even proposals with bundled items that are typically viewed as pro-shareholder may decrease shareholders' right to vote separately on each item. In this way, the Unbundling Rules are neutral regarding the desirable effects of individual proposals in that shareholders are empowered to make their own determination regarding a proposal's effects for each separately presented proposal.

However, as we will discuss in Part V, this classification is useful in identifying the subsample of bundled proposals that are more likely to receive negative recommendations from third party proxy voting services. That is, as we will see, proxy advisor firms appear to gauge their recommendation on what the advisor believes to be the aggregate impact of the bundled proposals rather than to take a principled position that bundling of material items calls for a negative recommendation. Given their apparent policies of recommending against a bundled proposal only when the net effect is negative, ISS and Glass Lewis will consider making a negative recommendation only if there is at least one item in the bundle that has a material adverse effect on shareholder rights. Hence, the subset of negative bundled proposals may be viewed as an upper bound of the number of cases where ISS and Glass Lewis may conclude that the net effect of the

145. *See supra* text accompanying note 98.

146. Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716, at *22–23 (S.D.N.Y. Feb. 22, 2013).

bundled proposal is negative and thus issue a negative recommendation. Later we question whether the aggregate impact approach that is taken by ISS and Glass Lewis is either principled or defensible.

IV. EMPIRICAL ANALYSIS: FREQUENCY OF BUNDLING

Having developed our four analytical classifications for investigating the presence of bundling, as well as sharply illustrating for each classification the policy considerations whereby each can be deemed to violate the Unbundling Rules, we next turn to applying them to the actual proposals that have been made in recent years. We begin by noting that there has been very little empirical work done on the prevalence of bundling and the likelihood of Unbundling Rules violations.[147] In this Part, we provide a detailed analysis of bundling using each of the definitions that we developed in Part III.

A. SAMPLE SELECTION

To create a sample for analysis, we use the ISS Voting Analytics ("VA") database,[148] which provides data about the items on the ballot at the annual meetings of Russell 3000 firms starting in 2003. In particular, for each item it provides a classification and description, management recommendation, ISS recommendations, and voting results. For the 2003–2012 period, VA includes 226,850 observations: 219,853 relate to management proposals—the subject of our study—and 6,997 relate to shareholder proposals.

Among the 219,583 management proposals in the VA database, 163,952 relate to director elections (each nominee is a separate item) and 23,972 are proposals to ratify the auditors. We do not examine these proposals because it seems unlikely that other items would be bundled with them (as confirmed by our reading of some proposals in these

147. In addition to Bebchuk & Kamar, *supra* note 34, which focuses on proposals related to mergers and acquisitions, there is an online student law review note that examines proxy statements in an attempt to determine the extent of bundling. Julian Ellis, Note, *The "Common Practice" of Bundling: Fact or Fiction*, 91 DENV. U. L. REV. ONLINE 105 (2014), http://www.denverlawreview.org/storage/online-article-pdfs/2014/proxy-issue/Ellis_Antibundling_Final-Format.pdf. In that online note, the author concludes that bundling does not actually occur all that often in practice. Using a sample of company proposals, the author found only one company other than Apple whose proxy statement "grouped together proposals that appeared significant." *Id.* at 116. It is not clear from the note how the author determines what exactly "significant" entails.

148. *Voting Analytics*, ISS, https://www.issgovernance.com/solutions/iss-analytics/voting-analytics/. All data obtained from the ISS Voting Analytics database are on file with authors.

categories).[149]

That leaves us with three main categories for analysis: charter amendments, M&A transactions involving mergers/consolidations, and executive compensation plans or related changes to the number of authorized shares of stock. Given that Bebchuk and Kamar have already analyzed the use of the Unbundling Rules in the M&A context,[150] we exclude another 1,082 proposals to approve a merger agreement or other transactions (for example, asset sales or share issuances made in connection with acquisitions). Also, we do not examine 22,507 compensation-related proposals (for example, mandatory say-on-pay votes, approval of different types of incentive plans) because the 2014 Interpretation exempts these types of proposals from the reach of the Unbundling Rules.[151]

The remaining sample includes 5,326 management proposals, of which 2,183 proposals are equity-related issues (such as proposals to increase authorized common stock) and 3,143 are management proposals related to governance provisions. Because it would be prohibitively costly to read and code all of these proposals, we focus on a subset of governance-related proposals that are described by ISS as involving an assortment of bylaw and/or charter amendments. ISS places proposals that it is unable to categorize as involving a single topic in these groupings. In particular, we focus on all the management proposals classified by ISS in the following categories:

M0126 - Amend Articles/Bylaws/Charter–Non-Routine (N=599);

M0267 - Company Specific–Board-Related (N=163);

M0106 - Amend Articles/Bylaws/Charter–Routine (N=87);

M0661 - Company-Specific–Organization-Related (N=68);

M0413 - Amend Articles/Bylaws/Charter–Organization-Related (N=34);

M0227 - Amend Articles–Board-Related (N=20);

M0602 - Amend Articles/Bylaws/Charter to Remove Antitakeover Provision(s) (N=14);

M0122 - Adopt New Articles of Association/Charter (N=12);

149. For the same reasons, we do not examine 1,344 proposals requesting to adjourn the shareholders' meeting in case the proxies required to vote for other items on the ballot at the meeting are not obtained (these proposals are usually the last item on the ballot at special meetings), and 844 items that ISS categorizes as "other business" (this is a generic category for proposals that may arise at meetings, such as shareholder proposals from the floor).

150. Bebchuk & Kamar, *supra* note 34.

151. As we said earlier, we disagree with the SEC's decision to exclude these proposals from the reach of the Unbundling Rules. We suspect that bundling is quite common in these proposals as they frequently seek shareholder approval for additional shares of authorized stock plus changes to equity incentive plans for executives.

M0378 - Amend Articles/Charter–Equity-Related (N=9);

M0660 - Amend Articles/Charter–Governance-Related (N=5);

M0377 - Amend Articles/Charter to Reflect Changes in Capital (N=3);

M0601 - Amend Articles/Bylaws/Charter to Include Antitakeover Provision(s) (N=2).

Coincidentally, there are exactly 1,000 proposals that fall within these categories. These proposals are particularly interesting to us because they capture situations where the opportunity to bundle arises naturally (for example, amending several different articles of the bylaws) and because ISS was unable to categorize them more specifically, which is perhaps (but not necessarily) an indication of their greater complexity and multiple items.

VA also gathers many types of governance-related management proposals within specific headings. For example, proposals are collected under headings for declassifying the board, reducing super majority voting requirements, changing the name of the corporation, and changing the state of incorporation. During our ten-year sample period, there were a total of 2,143 such specifically referenced governance-related proposals that appeared in fifty-six categories. In spite of the more precise categorization by ISS, it is still possible that these proposals bundle different items. To account for this possibility, whilst minimizing data collection costs, we examine the largest set of proposals in the fifty-six categories, namely the 520 proposals to declassify the board (ISS category M0215). These proposals are particularly important because of the importance of this anti-takeover defense to many shareholders and its documented association with firm value.[152] Also, these proposals are usually submitted by management in response to a non-binding shareholder proposal to declassify the board that won a majority vote the previous year(s) and, thus, they generally attract extremely high levels of shareholder support. As a result, they are of particular interest for our study because management may try to bundle these pro-shareholder proposals with other items viewed unfavorably by shareholders in order to get the less favorable items passed.

152. *See, e.g.*, Lucian A. Bebchuk & Alma Cohen, *The Costs of Entrenched Boards*, 78 J. FIN. ECON. 409 (2005); Alma Cohen & Charles Wang, *How Do Staggered Boards Affect Shareholder Value? Evidence from a Natural Experiment* (Harvard Bus. Sch. Accounting & Mgmt. Unit, Working Paper No. 13-068, 2013), http://ssrn.com/abstract=2141410.

B. HOW MUCH BUNDLING OCCURS?

After eliminating the various categories discussed above, our sample comprises 1,520 proposals (1,000 proposals relating to charter/bylaw amendments and 520 to declassify the board). For various reasons, such as missing SEC filings for some companies, we cannot obtain all of the necessary information to ascertain whether bundling takes place for 171 of these proposals. This leaves us with a final sample of 1,349 proposals. The first column of Table 1 below shows the annual distribution of these proposals from 2003 to 2012. The number of proposals peaks in 2008 at 205, although there are more than one hundred proposals in eight of the ten years in the sample. The remaining columns of Table 1 provide an overview of the frequency of bundling of items in these proposals using the alternative definitions of bundling introduced earlier in Part III. We discuss each of these categories in the sections below.

TABLE 1. Frequency and Type of Bundling

	No. of Management Proposals Examined	*No. (%) of "Generic" Bundled Proposals (% of Total Sample)*	*No. (%) of "Material" Bundled Proposals (% of Bundled Proposals)*	*No. (%) of "Multiple Material" Bundled Proposals (% of Material Bundled Proposals)*
2003	72	14 *(19.4%)*	12 *(85.7%)*	8 *(66.7%)*
2004	104	34 *(32.7%)*	27 *(79.4%)*	19 *(70.4%)*
2005	143	50 *(35.0%)*	41 *(82.0%)*	35 *(85.4%)*
2006	133	37 *(27.8%)*	31 *(83.8%)*	25 *(80.6%)*
2007	182	44 *(24.2%)*	41 *(93.2%)*	38 *(92.7%)*
2008	205	53 *(25.9%)*	37 *(69.8%)*	25 *(67.6%)*
2009	159	37 *(23.3%)*	32 *(86.5%)*	23 *(71.9%)*
2010	135	37 *(27.4%)*	30 *(81.1%)*	25 *(83.3%)*
2011	118	41 *(34.7%)*	32 *(78.0%)*	26 *(81.3%)*
2012	98	41 *(41.8%)*	34 *(83.0%)*	28 *(82.4%)*
Total Sample	1,349	388 *(28.8%)*	317 *(81.70%)*	252 *(79.5%)*

1. Generic Bundling

For each of the 1,349 proposals in our final sample, we carefully read the proposal description to identify all cases of generic bundling. As discussed above, generic bundling is the broadest definition of bundling and captures any proposal where the company has asked shareholders to approve more than one item with a single vote, regardless of whether the bundled items are technical, ministerial, or material. Thus, the frequency of generic bundling may be viewed as representing an upper bound of potential bundling violations in our sample.

As shown in the second column of Table 1, generic bundling is widespread during this ten-year time period, occurring in 388 cases and representing 28.8 percent of the total sample. In most sample years, the frequency of generic bundling cases ranges between 20 and 30 percent, with a minimum of 19.4 percent in 2003 and a maximum of 41.8 percent in 2012. This evidence suggests that at least this form of bundling is not limited to a handful of cases, as suggested in prior commentary.

2. Material Bundling

Generic bundling, however, does not necessarily violate the Unbundling Rules. As noted earlier in the discussion of *Greenlight Capital* as well as the 2014 Interpretation, the bundling of only "'ministerial or technical matters' that do not alter substantive shareholder rights" is not proscribed.[153] In order to differentiate between cases where the proposals solely involve immaterial ministerial or technical items ("housekeeping" matters) from situations where at least one item in the proposal has a material effect on shareholder rights, we next identify the subset of the 388 generic bundling proposals that fit within the definition of material bundling: that is, proposals in which at least one of the bundled items is of material importance to shareholders.

The results of this process are shown in the third column of Table 1. We classify 317 proposals as involving material bundling (the remaining 71 generic bundled proposals include only non-material items that are bundled). Material bundled proposals represent 81.7 percent of the generic bundled proposals, constituting almost one quarter (23.5 percent) of the overall sample. Stated differently, and with the caveat that our sample may have a relatively high frequency of bundling due to our selection process, nearly one in four management resolutions submitted to shareholders

153. Greenlight Capital, L.P. v. Apple, Inc., 2013 U.S. Dist. LEXIS 24716, at *15 (S.D.N.Y. Feb. 22, 2013) (quoting THOMAS & DIXON, *supra* note 62, at 9-23, 9-24).

within our ten-year sample entail material bundling. This is evidence of pervasive violations of the Unbundling Rules given that under the standard set forth in *Greenlight Capital*, any time a material item is bundled with additional items (material or not), this "violates the letter of the law."[154] Our evidence of the frequency of material bundling suggests violations of the Unbundling Rules are quite widespread, at least under this standard. We believe this reflects a significant level of noncompliance with the rules regulating proxies.

3. Multiple Material Bundling

Our third standard for Unbundling Rule violations is the one we denoted as multiple material bundling—that is, any case where two or more material items are bundled together in a single proposal for a vote. As noted earlier, there seems to be no dispute that multiple material bundling will violate the Unbundling Rules.[155]

Column 4 of Table 1 identifies the subset of material bundled proposals with more than one material item in the bundle. In our sample, 252 proposals fit this definition, representing 79.5 percent of the material bundled proposals, 64.9 percent of the generic bundled proposals, and almost one-fifth (18.7 percent) of the overall sample. This indicates that even under this more restrictive definition of bundling, a large number of proposals violate the Unbundling Rules.

C. WHAT TYPES OF PROPOSALS DO COMPANIES BUNDLE TOGETHER?

Having documented the widespread occurrence of bundling in our sample, we next look at what matters companies bundle on their ballots. As a first step, Table 2 below shows the frequency of each type of bundling across the main ISS proposal subcategories.[156]

154. *Id.* at *21–22 ("Permitting Apple to bundle numerous 'technical' matters with a single material matter would appear to still violate the letter of the law . . . .").

155. As noted earlier, the one exception would be the carve-out in the 2014 Interpretation for executive compensation plans. *See* 2014 Interpretation, *supra* note 81.

156. Table 2 categorizes proposals in accordance with the following ISS classifications: Amend Articles/Bylaws/Charter (M0126); Declassify the Board of Directors (M0215); Company Specific/Board-Related (M0267); Amend Articles/Bylaws/Charter-Routine (M0106); Company-Specific/Organization-Related (M0661); All Other Categories (M0122, M0227, M0377, M0378, M0413, M0601, M0602, M0660).

TABLE 2. Distribution of Frequency & Type of Bundling (ISS Categories)

Proposal Category	*No. of Management Proposals Examined*	*No. (%) of "Generic" Bundled Proposals (% of Total Sample)*	*No. (%) of "Material" Bundled Proposals (% of Bundled Proposals)*	*No. (%) of "Multiple Material" Bundled Proposals (% of Material Bundled Proposals)*
Amend Articles/ Bylaws/Charter -Non-Routine	515	126 *(24.5%)*	74 *(58.7%)*	55 *(74.3%)*
Declassify the Board of Directors	495	186 *(37.6%)*	186 *(100.0%)*	152 *(81.7%)*
Company Specific/ Board-Related	134	21 *(15.7%)*	21 *(100.0%)*	16 *(76.2%)*
Amend Articles/ Bylaws/ Charter -Routine	74	27 *(36.5%)*	20 *(74.1%)*	14 *(70.0%)*
Company-Specific/ Organization-Related	62	12 *(19.4%)*	8 *(66.7%)*	8 *(100.0%)*
All Other Categories	69	16 *(23.2%)*	8 *(50.0%)*	7 *(87.5%)*
Total Sample	1349	388 *(28.8%)*	317 *(81.7%)*	252 *(79.5%)*

Table 2 shows that the incidence of the various types of bundling is substantial across all the ISS categories that we examined. However, because the ISS classifications are, with the exception of the board declassification category, very general, the ISS breakdowns used in Table 2 shed little light on the actual content of most of the bundled proposals.

Thus, to gain a better understanding of the content of bundled proposals, we focus on the subset of material bundled proposals. We assign each of the material items bundled in them to a category that reflects its focus. In total, our sample of 317 material bundled proposals includes 613 material items,[157] corresponding on average to 1.93 material items per proposal (the number of material items per proposal ranges from one to five). To provide the reader with a sense of the potential implications of bundling, we also classify each material item as "Negative" or "Positive," depending on whether it decreases (Negative) or expands (Positive) shareholder rights. In doing so, consistent with the approach used to classify proposals as material, we rely on the current view of best practices in corporate governance (as reflected in the governance ratings, proxy advisors' voting guidelines, and voting policies of major institutional investors). Nonetheless, as discussed earlier, we acknowledge that the classification in some cases is subjective.

The results are reported in Table 3. For each item included in a material bundled proposal, Panel A presents the items that decrease shareholder power (Negative Items), and Panel B presents the items that increase shareholder power (Positive Items). The items in both panels are categorized as Board-related, Voting-related, Meeting-related, Takeover-related or Other. Board-related items refer to procedural rules regarding director selection and general director requirements. Voting-related items include changes that are related to board or shareholder voting. Meeting-related items refer to procedural rules relating to shareholder meetings, such as changes to advance notice procedures or rules governing quorum requirements. Takeover-related are those items that are directly related to raising or lowering the likelihood of a takeover.[158]

157. We classify the content of each bundled item rather than trying to classify types of bundled proposals per se because our sample contains very few bundled proposals that are completely identical.

158. If an item could be included in more than one category, we classify it in the category that seems most closely related to the item. For example, we classify a proposal to declassify the board as Takeover-related rather than Board-related.

TABLE 3. Panel A. Negative Items in "Material" Bundled Proposals

Board-related	
Expand indemnification D&O/limit personal liability	18
Enhance board authority in filling vacancies	9
Increase board power (vis-à-vis shareholders) in director removal process	7
Allow board to alter the number of directors without shareholder approval	5
Allow director removal only for cause	3
Other Board-related	11
Subtotal	50
Voting-related	
Eliminate/Restrict cumulative voting	11
Introduce supermajority voting requirements	3
Increase vote required to call a special meeting	1
Other Voting-related	11
Subtotal	26
Meeting-related	
Restrict advance notice procedures	8
Increase board authority regarding selection of meeting date/location	4
Increase quorum requirements	3
Other Meeting-related	3
Subtotal	18
Takeover-related	
Blank check preferred stock provision	6
Classify board	2
Other Takeover-related	3
Subtotal	11
Other	
Lack of clear information on the bundled item	10
Allow board to amend bylaws without a shareholder vote	7
Provide that shareholders may not act by written consent in lieu of a meeting	2
Add forum selection clause	1
Remaining items in the Other category	23
Subtotal	43
Total Negative Items	148

TABLE 3. Panel B. Positive Items in "Material" Bundled Proposals

Board-related	
Adopt majority voting for director elections	19
Increase shareholders' power (vis-à-vis the board) in director removal process	6
Enhance shareholder power in filling vacancies	2
Other Board-related	11
Subtotal	38
Voting-related	
Eliminate/Reduce Supermajority Voting Requirements	87
Decrease voting threshold for amendments approved by 2/3 of directors	2
Reduce voting threshold for special meetings	1
Other Voting-related	9
Subtotal	99
Meeting-related	
Make it easier to call a special meeting	3
Decrease quorum requirements	1
Increase notice period for meetings	1
Other Meeting-related	6
Subtotal	11
Takeover-related	
Declassify board	210
Allow directors to be removed without cause	92
Terminate poison pill	1
Other Takeover-related	2
Subtotal	305
Other	
Enhance shareholders' power to act by written consent	2
Increase shareholders' power to amend bylaws	1
Eliminate dual class stock structure	1
Remaining items in the Other category	8
Subtotal	12
Total Positive Items	465

Panel A of Table 3 shows that we identify 148 negative material items. Most of the negative items fall in the Board-related category (50 items), followed by Voting-related (26), Meeting-related (18), and Takeover-related (11). The most frequent negative bundled item is a provision to expand indemnification and/or limit personal liability for directors and officers (18 items). Other relatively frequent items are provisions eliminating or restricting cumulative voting (11 items), provisions enhancing board authority in filling board vacancies (9 items), provisions restricting advance notice procedures (8 items), provisions allowing the board to amend the bylaws without a shareholder vote (7 items), provisions increasing board power (vis-à-vis shareholders) in the director removal process (7 items), and blank check preferred stock provisions (6 items).

The Other category includes 10 cases we classify as negative because the proxy statement failed to disclose clearly what the shareholders were being asked to approve via the bundled proposal. An interesting example is NL Industries, Inc. where multiple technical items (for example, "(iii) remove certain provisions of the company's current certificate of incorporation that are similar to provisions of the New Jersey Business Corporation Act . . . (iv) make technical amendments to update the name and address of the company's registered agent and office")[159] were bundled with other items with potentially material but unclear implications for shareholders. These vague disclosures led ISS to note:

> ISS has concerns that the company's disclosure of the proposed amendments in its proxy statement does not specify such amendments' implications on shareholders' rights in regards to the amendment of Article VII, concerning shareholders' right to call special meetings . . . . Although the proposed amendments would update the company's charter to date, ISS recommends that shareholders vote AGAINST this proposal for lack of disclosure and potentially diminishing of shareholders' rights.[160]

The NL Industries example illustrates how bundling multiple items into a single proposal can obfuscate the implications of the bundled

159. INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING NL INDUS., INC. 14 (May 3, 2008). Although the SEC issued a comment letter noting a concern with this proxy statement, the comment was unrelated to the bundled proposal. *See* Letter from Terence O'Brien, Sec. Exch. Comm'n, to Harold C. Simmons, Chief Exec. Officer, NL Industries, Inc. (June 30, 2008), https://www.sec.gov/Archives/edgar/data/72162/000000000008032219/filename1.pdf.

160. INST'L S'HOLDER SERVS. (USA), PROXY REPORT REGARDING NL INDUS., INC. 14 (May 3, 2008).

proposal on shareholder rights.[161] It also illustrates why a legal standard that allows the bundling of a single material item with multiple technical and ministerial items (as the SEC permits in the 2014 Interpretation) would in practice be difficult to enforce, easy to abuse, and ultimately ineffective.

Next, Panel B shows that there are 465 positive material items, including 38 Board-related items, 99 Voting-related items, 11 Meeting-related items, and 305 Takeover-related items, with the remaining 12 items classified as "Other." Overall, the number of positive items is more than three times the number of negative items. However, this is largely because there were 210 proposals where board declassification was bundled with other items, such as an item allowing directors to be removed without cause (this particular bundle occurs in 92 cases).

If we temporarily disregard the 302 items that relate to the Declassify the Board of Directors (M0215) category from Table 2 (namely, board declassification (210) and director removal without cause (92)), we see that there are only 163 other positive material items that relate to charter and bylaw amendments categories (that is, all the categories in Table 2 other than M0215). This number is just slightly more than the 148 negative material items in those categories. Thus, in the portion of our sample that relates to charter and bylaw amendments (that is, excluding board declassification proposals and for-cause requirements to remove directors), companies appear to be bundling roughly the same number of positive and negative items. Comparing the composition of these remaining positive and negative items, the largest difference is in the Voting-related items, which contain a large number of positive items related to eliminating or reducing supermajority voting (87 proposals). We also note that of the 148 negative items, 37.2 percent (55 out of 155) were bundled in the same resolution with a positive proposal. That is, the classic form of distorted choice was present in this group more than one-third of the time.

There is no intrinsic need for these items to be bundled with other items. Indeed, in our work mining the VA database to collect our sample, we found abundant proxy statements where firms present virtually all the

161. Another example of this category is Proposal 3 from the 2010 Annual Meeting of Medifast, Inc. Medifast, Inc., Definitive Proxy Statement (DEF 14A), at 31 (Aug. 24, 2010), https://www.sec.gov/Archives/edgar/data/910329/000114420410046388/v194987_def14a.htm. This proposal requested that stockholders ratify changes to the company's bylaws, but the proposal did not describe the changes that shareholders were being asked to ratify. Nor did the proposal include the updated text of the bylaws. Instead, the proposal merely listed the reasons the board thought the change was necessary, such as the need to address "[f]alse reports about the Company by a group of convicted felons which negatively affected shareholder value by contributing to stock price volatility." *Id.*

items listed in Table 3 as separate, single-item proposals. In other words, companies are fully capable of presenting these proposals as separate items on their proxy statement.

V. EMPIRICAL ANALYSIS: SHAREHOLDER VOTING ON BUNDLED PROPOSALS

The final step in our analysis is to gather evidence on how proxy advisors respond to bundling, their recommendations in connection with bundled proposals, and how shareholders vote on bundled proposals. Previous studies document a strong correlation between shareholder votes and recommendations issued from ISS, the most influential proxy advisory firm, and, to a lesser extent, Glass Lewis, its closest competitor.[162] Across a variety of settings, such as shareholder proposals, say-on-pay votes, and director elections, an ISS or Glass Lewis recommendation is generally associated with 20–30 percent or 5–10 percent more votes, respectively, cast in line with the recommendation. Previous studies further document that the extent of proxy advisors' influence varies depending on the topics, the rationale underlying the recommendation, and the composition of the shareholder base (for example, proxy advisors' influence is more pronounced among smaller mutual funds with fewer resources and lower incentives to perform their own proxy analysis).[163]

In Table 4 we present data on the voting outcome of bundled proposals, the frequency of proxy advisors' positive and negative recommendations, and the association between such recommendations and voting outcomes. We report these data for the samples of generic bundled proposals, material bundled proposals, multiple material bundled proposals, and negative bundled proposals. This last category contains all material bundled proposals where at least one material item is "negative" based on the classification shown in Table 3. We identify 84 negative bundled proposals, representing 26.5 percent of the 317 material bundled proposals.

It is illuminating to evaluate proxy advisors' policies with regard to

162. For a description of the proxy advisory industry, see generally Stephen Choi, Jill Fisch & Marcel Kahan, *The Power of Proxy Advisors: Myth or Reality?*, 59 EMORY L.J. 869 (2010). For a review of the literature on shareholder voting, see Fabrizio Ferri, *"Low-Cost" Shareholder Activism: A Review of the Evidence*, *in* RESEARCH HANDBOOK ON THE ECONOMICS OF CORPORATE LAW 192 (Claire A. Hill & Brett H. McDonnell eds., 2012).

163. *See, e.g.*, Stephen J. Choi, Jill. E. Fisch & Marcel Kahan, *Director Elections and the Role of Proxy Advisors*, 82 S. CAL. L. REV. 649 (2009); Yonca Ertimur, Fabrizio Ferri & David Oesch, *Shareholder Votes and Proxy Advisors: Evidence from Say on Pay*, 51 J. ACCT. RES. 951 (2013); Peter Iliev & Michelle Lowry, *Are Mutual Funds Active Voters?*, 28 REV. FIN. STUD. 446 (2015).

bundling against the background of our negative bundling sample. As noted in Part II.C, ISS's policy is to recommend "for" the bundled proposal if the net effect of the different items is beneficial to shareholders and "against" if the net effect is perceived as detrimental to shareholder rights. Glass Lewis does not seem to have a general policy about bundling, but does in practice seem to follow something akin to the ISS policy. In other words, both ISS and Glass Lewis essentially make their voting recommendations on bundled proposals based on the perceived net effect of the items in the bundle. This implies that they will consider making a negative recommendation only if there is at least one item in the bundle that has a material adverse effect on shareholder rights. Hence, the subset of negative bundled proposals may be viewed as an upper bound of the number of cases where ISS and Glass Lewis may conclude that the net effect of the bundled proposal is negative and thus issue a negative recommendation.[164]

TABLE 4. Panel A. Voting Outcomes & Proxy Advisor Recommendations

Frequency of ISS Recommendations

Number of Proposals	"Generic" Bundled Proposals	"Material" Bundled Proposals	"Multiple Material" Bundled Proposals	"Negative" Bundled Proposals
All	388	317	252	84
... ISS recommends AGAINST	31 (8.0%)	31 (9.8%)	27 (10.7%)	31 (36.9%)
... ISS recommends FOR	357 (92.0%)	286 (90.2%)	225 (89.3%)	53 (63.1%)

164. As noted in Part II.C, in practice sometimes ISS appears to follow a different policy, issuing a negative recommendation if any of the bundled items would get a negative recommendation on a stand-alone basis. Even under this policy, our sample of negative bundled proposals represents a useful benchmark to examine in how many cases ISS concludes that the negative material item is significant enough to trigger a negative recommendation for the bundled proposal.

TABLE 4. Panel B. Voting Outcomes & Proxy Advisor Recommendations

Voting Outcome (Overall and by ISS Recommendation)				
Category	% Votes Against "Generic" Bundled Proposals	% Votes Against "Material" Bundled Proposals	% Votes Against "Multiple Material" Bundled Proposals	% Votes Against "Negative" Bundled Proposals
All	4.2%	4.7%	4.9%	13.6%
... ISS recommends AGAINST	25.7%	25.7%	25.8%	25.7%
... ISS recommends FOR	2.3%	2.5%	2.4%	6.1%

TABLE 4. Panel C. Voting Outcomes & Proxy Advisor Recommendations

Frequency of Glass Lewis Recommendations				
Number of Proposals	"Generic" Bundled Proposals	"Material" Bundled Proposals	"Multiple Material" Bundled Proposals	"Negative" Bundled Proposals
Subset of proposals for which GL recommendations are available	329	271	236	74
…GL recommends AGAINST	34 (10.3%)	31 (11.4%)	23 (9.7%)	27 (36.5%)
... GL recommends FOR	295 (89.7%)	240 (88.6%)	213 (90.3%)	47 (63.5%)

TABLE 4. Panel D. Voting Outcomes & Proxy Advisor Recommendations

Voting Outcome (Overall and by Glass Lewis Recommendation)

Number of Proposals	% Votes Against "Generic" Bundled Proposals	% Votes Against "Material" Bundled Proposals	% Votes Against "Multiple Material" Bundled Proposals	% Votes Against "Negative" Bundled Proposals
Subset of proposals for which GL recommendations are available	388	317	252	84
…GL recommends AGAINST	31 (8.0%)	31 (9.8%)	27 (10.7%)	31 (36.9%)
... GL recommends FOR	357 (92.0%)	286 (90.2%)	225 (89.3%)	53 (63.1%)

TABLE 4. Panel E. Voting Outcomes & Proxy Advisor Recommendations

Overlap Between ISS and Glass Lewis Recommendations on "Generic" Bundled Proposals

		Glass Lewis Recommends FOR	Glass Lewis Recommends AGAINST
ISS recommends FOR	No.	283	17
	% Votes Against	2.0%	9.4%
ISS recommends AGAINST	No.	12	17
	% Votes Against	26.1%	25.7%

TABLE 4. Panel F. Voting Outcomes & Proxy Advisor Recommendations

Overlap Between ISS and Glass Lewis Recommendations on "Negative" Bundled Proposals

		Glass Lewis Recommends FOR	Glass Lewis Recommends AGAINST
ISS recommends FOR	Num.	35	10
	% Votes Against	*3.9%*	*14.4%*
ISS recommends AGAINST	Num.	12	17
	% Votes Against	*26.1%*	*25.7%*

As shown in Panel A, ISS recommends a vote against 31 out of the 388 generic bundled proposals in our sample. Notably, all cases of "against" recommendations from ISS involve proposals that we code as negative bundling, which provides support for our coding classification. These 31 cases of ISS "against" recommendations, while constituting only 8.0 percent and 9.8 percent of the generic and material bundling sample, respectively, represent 36.9 percent of the negative bundling cases. This figure is of particular interest because, as discussed earlier, the negative bundling sample represents the upper bound of the number of "against" recommendations potentially issued by proxy advisors. The reason why ISS issues an "against" recommendation for only 31 of the 84 (36.9 percent) negative bundled proposals, with the remaining 53 proposals receiving a "for" recommendation, is that many of these negative bundled proposals also contain positive items (such as a proposal to declassify the board or to adopt majority voting) and ISS assesses the net effect to be positive for shareholders.

We also examine how frequently ISS's analysis of the proposal explicitly mentions its bundled nature.[165] In untabulated results, we find that ISS highlights the bundled nature of the proposal in only 12.9 percent of the generic bundling sample. We conjecture that this low frequency occurs because ISS only mentions bundling when it involves material (or material negative) items. However, even in the subsample of material and material negative bundling, the frequency of cases where the ISS report explicitly alerts shareholders about the bundled nature of the proposal

165. We do not have access to the Glass Lewis reports. Hence, we performed this analysis only for the ISS reports.

remains low at 15.4 percent and 28.2 percent, respectively. It is consistent with the fact that bundling per se does not trigger a negative ISS recommendation, but it also means that shareholders cannot rely on ISS's analysis to identify bundled proposals. We deduce from this that ISS does not accord bundling much weight when evaluating bundled proposals.

Panel B reports data on the voting outcome. On average, the percentage of votes against generic bundled proposals [hereinafter voting dissent] is fairly low, at 4.2 percent. However, when ISS recommends against the proposal, negative votes increase to 25.7 percent, confirming the strong association between voting outcomes and ISS recommendations documented in prior studies on shareholder voting. This association, combined with the fact that all the "against" recommendations from ISS involve cases of negative bundling, explains the higher average voting dissent for the negative bundling subsample (13.6 percent versus 4.2 percent for all bundling cases). While not reported in Panel B, we note that 7 of the 31 proposals with negative ISS recommendations failed to pass because they did not achieve the required majority, or supermajority, vote. This constitutes further evidence of the potential impact of ISS recommendations on voting outcomes. The lack of shareholder approval may also suggest that managers deployed bundling to avoid exactly what did occur: failure of the shareholders to approve the negative impact proposal. Indeed, the presence of bundling in connection with any negative material proposals raises concern of whether bundling moved the needle toward shareholder approval at least from what it would have been had the material negative item not been bundled. This concern is all the greater in light of the decision by the largest proxy advisory firm, ISS, to issue recommendations based on the net impact of the proposal, thus allowing companies that bundle negative items to potentially receive favorable voting recommendations.

In Panels C and D of Table 4, we present similar data for the subset of 329 generic bundled proposals for which we were able to obtain Glass Lewis recommendations. While we only have access to Glass Lewis recommendations for the 2004–2011 period, the pattern is generally similar to the one reported in Panels A and B for ISS. The frequency of "against" recommendations from Glass Lewis in the generic bundling sample is 10.3 percent, increasing to 11.4 percent in cases of material bundling and 36.5 percent in cases of negative bundling (Panel C). On average, voting dissent for generic bundled proposals is low, at 4.5 percent, but it increases to 18.1 percent when Glass Lewis recommends against the proposal. This increase is more pronounced for the negative bundling cases, where an "against" recommendation from Glass Lewis is associated with an average voting dissent of 22.1 percent (Panel D).

Moving on to Panel E, for the subset of 329 bundled proposals with both ISS and Glass Lewis recommendations available, we also report the frequency of cases where one or both of the proxy advisors issue an "against" recommendation, and the associated voting outcome. It appears that there is significant "disagreement" between the two advisors: out of the 46 cases (= 17+17+12) where at least one of them recommends against the proposal, they "agree" (both recommend 'against') only in 17 cases (37.0 percent).[166]

The contrasting positions of ISS and Glass Lewis shine a light on how even expert proxy advisors can reach different conclusions when evaluating the net effect of bundled proposals, perhaps because of the confusing disclosures and complex nature of many of these bundled proposals. This lack of concordance supports our earlier position that the benefits or detriments of a particular proposal are difficult to determine ex ante. Hence, our position is that it is far better to favor separate treatment so that the proof of the pudding can be its tasting. If each material proposal was the subject of a separate shareholder vote, we would expect much greater consistency in these recommendations. As explained earlier, the Adopting Release and *Koppel* each make the case for a strong presumption of separate treatment. This is also indirect evidence of the weakness of the current SEC regulations related to the Unbundling Rules because even experts applying similar standards appear to disagree on the full implications of many of these proposals.

Panel E also shows that the association between recommendations and voting outcomes is much more pronounced for ISS recommendations than for Glass Lewis recommendations. For example, when Glass Lewis recommends in favor of the proposal, an "against" ISS recommendation is associated with a 24.1 percent increase in voting dissent (from 2 to 26.1 percent). In contrast, when ISS recommends in favor of the proposal, an "against" Glass Lewis recommendation is only associated with a 7.4

166. In Panel F, we repeat the analysis in Panel E for the subset of 74 bundled proposals classified as cases of negative bundling and with available data on both ISS and Glass Lewis recommendations. The results are generally similar. Out of the 39 cases (= 17+10+12) where at least one of the proxy advisors recommends against the proposal, they "agree" (both recommend "against") in 17 cases (43.6 percent). The association between recommendations and voting outcomes continues to be more pronounced for ISS recommendations, and there is very limited shareholder scrutiny of proposals that do not receive an "against" voting recommendation from at least one proxy advisor (voting dissent in these cases is only 3.9 percent).

percent increase in voting dissent (from 2 to 9.4 percent). This evidence is consistent with prior studies[167] and can be explained by the fact that ISS has a much larger client base.[168]

The other important insight from Panel E is that voting dissent when neither of these proxy advisors recommend against a bundled proposal is only 2.0 percent. This suggests that institutional investors give little scrutiny to bundled proposals unless they are singled out by proxy advisors for negative recommendations. Hence, it becomes even more important that proxy advisors revise their policy guidelines regarding bundling.

CONCLUSIONS AND POLICY RECOMMENDATIONS

When the SEC adopted the Unbundling Rules in 1992, it acted to fulfill the shareholder franchise by enabling shareholders to better convey their views to boards of directors; by so acting, the SEC also protected against corporate management distorting shareholders' choices in a way that led investors to mistakenly approve items that they did not truly want to enact. The need to protect the shareholder franchise from these evils is just as strong today as it was then.

During the past twenty plus years, the courts have tried to insure that the Unbundling Rules are interpreted in a manner that is consistent with this intention in their decisions. In the *Koppel* and *Greenlight Capital* decisions, the courts developed sensible rules based on thoughtful interpretations of the Unbundling Rules. However, the SEC did not pay sufficient attention to these judicial decisions and instead has undermined the integrity of these rules with its interpretive releases. These releases have both exempted large categories of shareholder proposals from the reach of the Unbundling Rules without any explanation and created vague criterion for evaluating the remaining proposals. The ambiguous standards proposed by the SEC make it easy for companies to avoid shareholder scrutiny and distort investor choices. Proxy advisors have contributed to the failure to enforce the Unbundling Rules by employing analytical techniques in evaluating management proposals that fail to deter violations. In the remainder of this section, we briefly outline some ways in which the SEC, third party voting advisors, and institutional investors can better implement

167. *See, e.g.*, Ertimur, *supra* note 163.

168. Scott S. Winter, Director, Innisfree M&A Inc., Trends in Shareholder Voting – The Impact of Proxy Advisory Firms, Presentation at Am. Bar Ass'n Corp. Governance Comm., at 1 (Oct. 12, 2010), http://apps.americanbar.org/buslaw/committees/CL260000pub/materials/20101012/TrendsShareholderVoting.PDF ("ISS clients typically control 20–30 [percent] of a midcap/largecap corporation's outstanding shares. Glass Lewis clients typically control 5–10 [percent] of such shares.").

the Unbundling Rules.

First, we recommend that the SEC withdraw its 2004 Guidance, the 2015 Interpretation, and the 2014 Interpretation, and replace them with a simpler, more transparent, standard. In particular, the SEC should act consistently with the court decisions so that any material proposal must be separately presented. Furthermore, it should discard the vague and easily abused "inextricably intertwined" exemption for complex proposals, which presents an invitation for abuse, and eliminate the exemption for executive compensation proposals. In its place, the SEC should clearly and narrowly define what kinds of matters are not separate. For example, the SEC should carefully set forth rules of what constitutes a recapitalization in a manner consistent with the analysis developed above.

Second, we propose that the SEC at least adopt the material bundling definition that we developed in Part III.B to determine when a proposal needs to be presented separately to the shareholders. This test is less strict than the generic bundling test, but more stringent than the multiple material bundling standard, both of which are discussed in that same section. The material bundling test is consistent with the judicial guidance given in *Greenlight Capital* and, as reasoned earlier, is consistent with the materiality standard commonly employed in addressing the information needs of shareholders voting on proxy matters. While it is likely to slightly increase the number of items that are presented as separate proposals to shareholders on the corporate ballot, its advantages far outweigh the relatively small costs associated with that increase. The material bundling test will do a far better job of presenting shareholders with undistorted choices that allow them to freely express their preferences to corporate boards.

Third, we propose that the standard for determining a proposal's materiality be expanded to include any matter whose initiation or amendment, as a matter of state law, requires the concurrence of the shareholders. This change is rooted in our discussion earlier that proxy rules should complement rather than trivialize state corporate law, at least when it comes to the rights of shareholders to communicate their views on a single proposal.

Fourth, we urge the third party voting advisors to stop ignoring violations of the Unbundling Rules in making their voting recommendations. As advocates for their institutional investor clients, they need to adopt strict policies of issuing "against" recommendations on any management proposal that violates the Unbundling Rules. If they made such a change, and the SEC adopted the material bundling standard we suggest, third party voting advisors would be much better able to provide their clients with clear voting guidance. This would deter companies from violating the Unbundling Rules and lead to better enforcement of them.

Finally, institutional investors need to demand these changes. The SEC has shown in the past that it will respond to informed shareholder pressure to enforce its rules. Collectively, the institutional investors should make it clear that the Unbundling Rules are an important part of protecting the shareholder franchise. They should also clarify their voting policies to make it clear that they will vote against all improperly bundled proposals. This would also have the advantage of making it clear to the third party voting advisors what their clients consider important.