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ABA Committee Proposes New Majority Voting Solution

The American Bar Association Committee on Corporate Laws has issued a preliminary report on director elections in which it offers a novel approach to majority voting. The report recommends changes to the Model Business Corporation Act designed to balance activist-shareholder demands for majority voting with the need for certainty and avoiding failed elections.

Under the ABA Committee proposal, directors would continue to be elected by a plurality vote, but a company's board or shareholders would be able to adopt a bylaw that would give effect to majority voting in director elections. The shareholders of a company that adopts the proposed bylaw would be able to vote for or against director candidates (or to abstain) and a director who is elected by a plurality but who fails to receive more for votes than against votes would serve for a 90-day term (subject to earlier replacement by the board). At the end of the 90-day period, the board could reduce its size or elect a director to fill the vacancy. The candidate who was rejected by the shareholders would be eligible for reappointment by the board, although for practical reasons reappointment would be unlikely. As currently proposed, this bylaw if adopted would apply in contested and uncontested elections.

The ABA Committee proposal also would permit companies to opt out of plurality voting by charter amendment, which requires board and shareholder action. Finally, the ABA Committee also proposes a clarification to the law to remove any doubts regarding the validity of a Pfizer-type board policy on director election.

The ABA Committee proposal is a thoughtful addition to the debate on majority voting. One significant concern with the proposal, however, is its failure to carve out proxy contests (where a third party is soliciting proxies for one or more candidates other than those recommended by the board). We believe that majority voting is not only unnecessary in contested elections, where plurality voting is generally considered to be appropriate, but its application in that context could raise a variety of potential complications.

We continue to believe that majority voting will become universal and that the Pfizer-type board policy is the best way to achieve majority voting, ISS to the contrary notwithstanding. The ABA Committee proposal offers a way to give greater effect to shareholder concerns without the risk of failed elections. The ABA Committee is seeking comments on its proposals and it will be some time before they might become law. Companies seeking an acceptable solution may wish to consider implementing a version of the proposed bylaw providing that directors who receive more against votes than for votes will serve only the truncated 90-day term. Such a bylaw should not apply to contested elections.

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