

Navigating Proxy Season Amid Uncertainty: **New SEC Staff Guidance on “Passive Investor” Status May Complicate Shareholder Engagement Efforts**

Key Takeaways

On February 11, 2025, the SEC staff issued two updates to its Compliance and Disclosure Interpretations, or C&DIs, addressing Schedule 13D/G beneficial ownership filings. The full impact of this guidance remains uncertain, but at present some major institutional investors have paused engagement activities with certain portfolio companies. As we are heading into peak proxy season, this guidance may impact companies’ abilities to engage with their largest investors as they have in years past.

Immediate Implications for Companies

- 1** Large institutional investors may decline to engage with companies where the investor’s beneficial ownership position exceeds 5%
- 2** In the absence of the opportunity for in-season dialogue with key investors
 - It will be increasingly important for a company’s proxy disclosure to clearly communicate the rationale for compensation decision-making
 - Supplemental proxy materials may need to more explicitly home in on key messages
- 3** Companies may need to engage with smaller investors (or enhance retail investor engagement) in connection with close or contentious votes

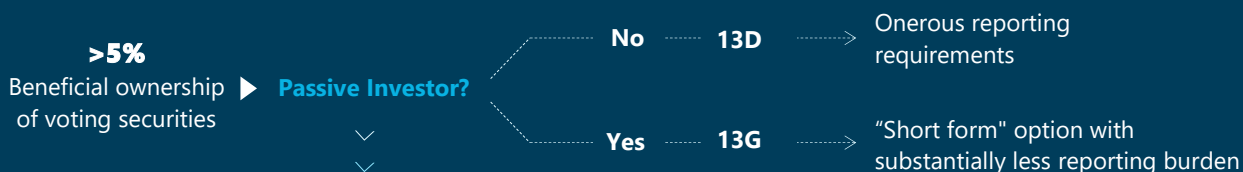
Background: Schedules 13 D and G

In short, shareholders that beneficially own more than 5% of a company’s voting securities are required to report their ownership with the SEC. That reporting must be done via Schedule 13D – which entails relatively onerous reporting requirements – unless the shareholder is eligible for an exemption that permits use of Schedule 13G, a “short form” filing that requires substantially less information. Those exemptions require that the investor be “passive” – i.e., they did not acquire the securities with the purpose or effect of changing or influencing the control of the issuer. Historically, large institutional investors like BlackRock, Vanguard, Fidelity and the like have relied on those exemptions to avail themselves to scaled back Schedule 13G filings.

What’s Changed?

The new and revised C&DIs provide updated guidance on what the SEC staff considers to be a passive investor. Previously, ordinary course engagement on topics such as corporate governance, executive compensation, and environmental or social issues would generally not preclude finding that an investor is “passive.” The new guidance indicates that if, in the course of such engagements, an investor “exerts pressure” on management to make specific changes to policies or practices, or indicates its support for a company’s director nominees may be withheld absent change that aligns with the shareholder’s expectations, it may no longer use Schedule 13G. Accordingly, investors are now assessing their engagement practices and voting guidelines relative to this new guidance, that leaves much open for question and interpretation.

Beneficial ownership reporting update



Status Change

Previously

Ordinary **engagement** on corporate governance, executive compensation, and environmental or social issues **would not preclude passive investor classification.**

Latest SEC update

If an investor, during engagement on corporate governance or other issues **“exerts pressure”** on management to implement specific policy or practice changes or takes actions that influence company control, they **will no longer qualify as a passive investor.**

Impact

Institutional investors are now:

- Reassessing their engagement practices
- Reviewing their voting guidelines
- Navigating considerable interpretative uncertainty

Need Assistance?

Compensia has extensive experience in helping companies establish executive compensation programs and practices and developing disclosure of such practices in their proxy materials taking into consideration SEC disclosure requirements, proxy advisor policies and investor expectations. If you would like assistance with or if you have any questions on the subjects addressed in this Thoughtful Disclosure Alert, please contact your regular Compensia team members or the authors of this Alert:

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About Compensia

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