Cisco Investors to Vote on Proxy Advisor Contest Proposal

By Ian Thomas  September 3, 2013

Amid the criticism of the proxy advisory firm industry, a governance advocate has recently proposed a potential solution on how to improve the effectiveness of the reports: Hold a contest.

A recent shareholder proposal filed at Cisco asking for a competition among proxy advisors to give advice on how to vote at the company’s annual general meeting in 2014 was approved by the SEC on August 9.

The proposal, submitted by Jim McRitchie, publisher of CorpGov.net, a shareholder interest group, would help spur competition and increase the quality of proxy advising, which is currently dominated by ISS and Glass Lewis, he says.

“Many directors and shareholders have complained about proxy advisors not doing a good enough job, so if they’re not going to do a good job, let’s try a new model,” McRitchie says.

Under the proposal, Cisco shareholders would vote in the 2014 proxy on which four advisors provided what McRitchie describes as “the most useful voting advice.” The company would award those winners cash prizes totaling up to no more than $50,000. In order to insulate advisor selection from influence by Cisco’s management, any person or organization could enter by paying a fee.

While this is not the first time McRitchie has suggested such a contest, it is the first one to require advisor analysis of the board of directors and the individual effectiveness of each member.

McRitchie believes that opening the competition to provide analysis may encourage industry experts and “insider types” to provide their thoughts on the contributions of the different directors.

“The hardest votes that many shareholders have is voting for directors, and most just wonder, ‘How in the hell do I know what directors are doing the right thing and which are not?’” he says.
“At Cisco, the company traded at a heavier premium to the broader market a decade ago. Now, it’s trading at a discount and the enterprise-technology market has changed drastically,” McRitchie adds. “There should be a question if today’s board is savvy enough to move the company forward.”

Cisco aimed to omit the proposal from its proxy card, filing a no-action request with the SEC, where it argued that the selection of a winner would be a “game of chance” and that it could affect the outcome of the company’s director votes, as well as not establishing a standard that would be used to evaluate the entries.

But the SEC disagreed, and the proposal will be put to a vote at its November 11 annual general meeting. A Cisco spokesperson confirmed that the company had received the proposal, but since it has not yet filed its proxy, neither the company nor the board would comment further on the matter.

But even if the proposal receives some shareholder support at that meeting, it is still uncertain what sort of value this contest would bring, says **Jim Barrall**, a partner at **Latham & Watkins**.

"Individuals and smaller proxy advisors likely would not find anything new or unusual, make any different arguments, or shed any new light on executive compensation or governance matters,” Barrall says. “Investors are already inundated with information; larger institutional investors wouldn’t even bother to read it, and frankly it would create a bit of a side-show.”

Barrall says allowing for essentially anyone to provide analysis would only encourage those activists with specific agendas to promote their views to the larger shareholder group as a whole.

“We’ve seen companies file supplementary filings to contest what **ISS** or **Glass Lewis** has had to say; this could present situations where the company could face any kind of allegation, and it would have to make a decision to contest them or not,” he says. “It already takes companies plenty of time and money to run through this process; I don’t see enough value here for it to catch on.”

**Keir Gumbs**, a partner at **Covington & Burling**, says that he is surprised that Cisco did not challenge the proposal on the argument that it relates to ordinary business operations. Both Amazon and Costco omitted similar proposals from being voted on in 2013 using that argument, noting that the proposal would “seek to micromanage the company to such a degree that exclusion of the proposal is appropriate.”

“Shareholders may have some dissatisfaction regarding the advice of the bigger proxy advisory firms, but issuers don’t have anything to do with who the shareholders rely on,” says Gumbs. “If it were up to the issuers, the shareholders would likely just deal directly with them.”

While McRitchie says he is unsure of how much support the proposal will receive from shareholders, he notes this sort of process can begin a debate over advice that shareholders are given, which often comes from advisory firms with a limited, “one-size-fits-all approach.”
“Directors should embrace a system like this because it will allow them to do things that just aren’t standard procedure and look outside the box for the best ways to approach issues,” he says. “Many of the advisory firms have a best practices–type check box for each director, and a contest like this would allow for a director and board to try things that aren’t just considered best practices and be praised for it.”