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Nov. 9, 2021, 6:01 AM

- SEC policy shift to empower investor proposals in 2022
- Companies won't get to rely on past exclusion decisions

Companies will need fresh ways to fend off activist shareholders in next year's proxy season on issues like climate change and social justice, after the SEC made it harder to exclude ballot proposals from annual corporate meetings.

The Securities and Exchange Commission will impose tighter scrutiny on companies that use traditional ballot-battle tactics—such as relying on their prior arguments and past SEC decisions to win the agency's support—to quash shareholder proposals on environmental, social and governance issues. The agency announced the changes to its no-action letter policy last week.

The move reflects the agency's heightened emphasis on corporate ESG disclosures, in line with the Biden administration's priorities on social issues. The changes will leave many companies with far fewer options for quashing shareholder proposals. But more emboldened activist shareholders will likely gain an edge in getting proxy votes.

Companies hoping to head off proxy votes will need to be more proactive and specific about what they're already doing to tackle ESG issues, said Patrick Gadson, a partner at Vinson & Elkins LLP in New York who co-leads the firm's shareholder activism practice.

That includes more detailed ESG disclosures on company websites and SEC filings, he said.

“You’re going to have to lay out a case that you really are doing this in a very specific, granular way and hope that the [SEC] staff respects that,” he said.

The SEC said Nov. 3 that it will give less credence to corporate arguments that social policy issues, such as climate or workforce diversity proposals, are inappropriately intrusive and would interfere with a company’s “ordinary business” operations.

Companies facing a shareholder proposal typically look to other companies’ that have had success in getting SEC support to defeat a similar proposal. These companies then often cite these past examples to urge the SEC to issue a similar no-action letter.

But prior-year precedent “is no longer going to be helpful,” said Christina Thomas, a partner at Mayer Brown LLP in Washington and former counsel to SEC Commissioner Elad Roisman, a Republican.

The agency cited its recent rejection of ConocoPhilips’ request to nix a shareholder proposal for the oil company to set targets for greenhouse gas reductions. The SEC said the ballot proposal didn’t qualify for a “micromanagement exclusion” that would nix a vote because it didn’t impose specific methods for the company to cut emissions.

The SEC said it will now consider broader social policy considerations when deciding a proxy exclusion request, rather than just focusing on a proposal’s specific impact on a company.

Eventually, a new pattern will likely emerge on how the SEC, under its new policy, issues its no-action letters that allow companies to quash shareholder proposals. Companies will particularly pay close attention to the ones who have success early on in convincing the SEC.

“The first actor in that space will be very helpful for everyone else,” Gadson said.

Activist Edge

The SEC changes “empowered shareholders to pursue ESG proposals at their companies,” according to the Shareholder Rights Group, which represents activist investors and socially-minded asset managers.

Companies that relied heavily in the past on arguments that shareholder proposals don't directly relate to their business might forego SEC requests and just allow proxy votes, Thomas said.

But other companies may not be deterred so easily in their attempt to remove proposals.

Companies that are proactive about publicly disclosing shareholder-priority issues—like workplace diversity efforts or greenhouse gas reductions—would likely face fewer proposals related to them, Gadson said. Such companies also may find it easier to get the SEC's support to nix such proposals if they get one, he said.

Companies can still make "micromanagement" arguments about proxy proposals on climate or diversity, but their case would be stronger if they pointed to their public disclosures about those same issues, he said.

Companies "need to get out in front of all this" by showing the SEC they're already tackling those issues, Gadson said.

Biden Priority

The Nov. 3 bulletin comes as the SEC works to propose rules in the coming months that could have companies report their climate risk in their annual 10-Ks or other public filings.

ESG-focused policymaking is front and center at other agencies as well. The Department of Labor recently issued a proposal to make it easier for retirement savers to consider ESG criteria in their investment decisions.

"We are seeing the Biden administration making some moves to make it easier for shareholders to engage in ESG activism," said Sarah Haan, professor at Washington and Lee University School of Law.

The U.S. Chamber of Commerce called for the SEC to reverse its decision.

The policy threatens "to turn board rooms and shareholder meetings into political debate societies on issues the SEC admits have no nexus to the actual business of the company," Thomas Quaadman, executive vice president of the Chamber's Center for Capital Markets Competitiveness, said in a public statement.

The Shareholder Rights Group said the proxy changes will reduce long-term costs and uncertainties for companies and their shareholders by forcing them to address issues like climate and diversity sooner rather than later.

The SEC’s move is also important for advancing transparency in corporate political giving, said Bruce Freed, president of the Center for Political Accountability.

During the Trump administration, the SEC often granted no-action letters to companies seeking to exclude proxy votes on corporate donations to trade groups and political action committees, Freed said.

“There will be fewer grounds for companies to challenge resolutions that call on companies to look at issues much more broadly,” he said.