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3 Corporate Governance Trends To Watch This Proxy Season

By **Lisa Silverman** (April 7, 2021, 5:59 PM EDT)


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While the 2021 proxy season is just beginning, several intersecting trends are emerging that could have an impact for years to come.

Early data show[1] that U.S. corporations are fighting harder than ever to keep shareholder proposals off the ballot, while the U.S. Securities and Exchange Commission has issued a series of notices indicating that environmental, social and governance, or ESG, issues will be a priority this year. And after a year of disappointing results, some corporate boards are abandoning their commitment to performance-based metrics.

The convergence of these three trends will no doubt make the proxy season of 2021 one to watch. It's going to be a wild ride as Main Street and Wall Street collide in a pandemic-battered country.

Challenges to Proxy Voting and Permission to Skip Votes

In 2020, Trump administration appointees to the SEC made it more difficult to for shareholders to force a vote at an annual meeting by amending Exchange Act Rule 14a-8, which previously let investors put forth a proposal if they owned at least $2,000 or 1% of a public company's voting shares for at least one year.[2]

Under the amended rule, the length of time a shareholder must hold a company's securities varies depending on the amount owned. The amended rule also makes it easier for a company to exclude a proposal from its proxy statement if the proposal previously failed to receive support.

As of March 15, companies have asked the SEC for permission to skip votes on 33% of the year's 437 shareholder resolutions, up from 27% in 2020.[3]

As some companies seek to exclude shareholder proposals calling for racial equity, President Joe Biden's designate as acting head of the SEC, Allison Herren Lee, has said the commission plans to review rules on proxy voting and possibly revise how companies ask to skip votes.

With this planned review, the SEC is renewing the commitment it made to investors during the Obama administration to empower corporations and their investors to be able to vote on proposals that matter to them by assessing whether the proxy voting process promotes or impedes shareholders rights.

Those on both sides of the current rule are likely to argue that their position is in the best interest of all and will be marshalling their arguments to appeal to shareholders and regulators.

Climate Change and ESG Take Center Stage

In a March 15 speech, Lee made clear that climate change and ESG were "front and center for the SEC," stating:

> Human capital, human rights, climate change — these issues are fundamental to our markets, and investors want to and can help drive sustainable solutions on these issues.

Lee also indicated that the SEC was considering new rules for public company disclosure, noting:

> Investors are demanding more and better information on climate and ESG, and that demand is not being met by the current voluntary framework. ... Not all companies do or will disclose without a mandatory framework, raising the cost, or resulting in the misallocation, of capital.[4]

Lee stated she was asking the SEC to solicit public input on how to require companies to disclose "consistent, comparable, and reliable information on climate change." The commission's Asset Management Advisory Committee has already issued a preliminary recommendation that the SEC require standards for companies to disclose material ESG risks.[5]

On the heels of Lee's speech the Commodity Futures Trading Commission announced it was establishing a Climate Risk Unit to focus on the role of complex financial derivatives in understanding climate related hazards.[6] And on April 5 in remarks before the Chicago Council on Global Affairs, U.S. Treasury Secretary Janet Yellen called climate change, "the biggest long-term threat the world faces," echoing and amplifying comments she made during her confirmation hearings.[7]

These comments and actions signal that new disclosures regarding climate risks and remediation may be coming soon. As we saw more than a decade ago when the say-on-pay resolution was making its way through the SEC, before, not after, passage is the time for companies to assess their strengths and vulnerabilities and begin to make preparations for future requirements.

We are seeing these issues play out in real time in the current proxy fight between ExxonMobil Corp. and newly formed activist fund, Engine No. 1 GP LLC, which among other things is pushing the company to set a net-zero climate goal.

Changes to Executive Compensation Criteria

In addition to keeping an eye on ESG issues, shareholders are closely monitoring executive compensation. In recent years, this metric has been tied closely to company performance; however, in 2020, some companies decoupled this metric.

Under its performance metrics, three senior executives at Walgreens Boots Alliance Inc. did not qualify for an annual bonus for 2020 but received one anyway.[8] And in its August 2020 proxy, Darden Restaurants Inc. said it excluded the quarter that ended May 31, 2020, when it calculated its cash awards.[9]

Investors will have the opportunity to weigh in on these decisions, since 2021 marks the 11th year companies must seek nonbinding approval on executive compensation from their shareholders. These say-on-pay votes typically pass with more than 80% approval. However, this year, shareholders are not as happy with corporate compensation during the pandemic.

At least one company — Starbucks Corp. — has already made news this proxy season when shareholders voted against the company's say-on-pay proposal at the company's 2021 annual meeting.[10] And at its AmerisourceBergen Corp.'s March 11 annual meeting, the say-on-pay vote barely passed, with two major hedge funds voting in opposite ways.[11]

All of this signals investors are closely evaluating companies' decisions to follow their own guidelines with respect to executive compensation. As the 2021 proxy season continues, we can expect investors to continue to hold accountable corporations that ignore their previously stated policies.

Based on early trends, companies facing activist pressure are likely to find themselves doing battle on several fronts and will need to be strategic in assessing and responding to the range of activist demands.

Those that are not currently facing activist demands should use this time to inoculate themselves against future pressure by engaging with shareholders on a regular basis. These actions will enable corporations and their boards to heed the clarion call of investors to ensure that what is profitable is also good, while creating long-term value and sustainability.

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[1] Reuters, 18 March 2021: https://www.reuters.com/article/us-usa-race-investors-focus/u-s-corporate-reformers-face-more-fights-to-get-proxy-votes-idUSKBN2BA2FN.

[2] SEC, 23 September 2020: https://www.sec.gov/news/press-release/2020-220.

[3] Reuters, 18 March 2021: https://www.reuters.com/article/us-usa-race-investors-focus/u-s-corporate-reformers-face-more-fights-to-get-proxy-votes-idUSKBN2BA2FN.

[4] SEC, 15 March 2021: https://www.sec.gov/news/speech/lee-climate-change.

[5] SEC, 1 December 2020: https://www.sec.gov/files/potential-recommendations-of-the-esg-subcommittee-12012020.pdf.

[6] CFTC, 17 March 2021: https://www.cftc.gov/PressRoom/PressReleases/8368-21.

[7] U.S. Department of the Treasury, 5 April 2021: https://home.treasury.gov/news/press-releases/jy0101.

[8] Walgreens Boots Alliance/SEC, 28 January 2021: https://www.sec.gov/Archives/edgar/data/1618921/000120677420003147/wba3796681-

def14a.htm.

[9] Darden Restaurants/SEC, 23 September 2020: https://www.sec.gov/Archives/edgar/data/940944/000094094420000053/def14a2020definitiveproxys.htm.

[10] Starbucks/SEC, 17 March 2021: https://www.sec.gov/ix?doc=/Archives/edgar/data/829224/000119312521087492/d152191d8k.htm.

[11] AmerisourceBergen/SEC, 11 March 2021: https://www.sec.gov/ix?doc=/Archives/edgar/data/1140859/000114085921000015/abc-20210311.htm.