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UNIVERSAL PROXY AND TRENDS IN SHAREHOLDER ACTIVISM: CORPORATIONS MUST STILL BEWARE AND TAKE CARE

Shareholder activism remains a prevalent phenomenon in the U.S. markets with no signs of abating. The contours of shareholder activism have been impacted by several developments, including the advent of the universal proxy card system. Companies must be well prepared in advance for shareholder activism generally, and they should specifically prepare to strategically manage and leverage the universal proxy card in the event of a proxy contest.

By Derek Zaba, Kai H.E. Liekefett, and Leonard Wood *

As the 2024 proxy season drew to a close, a foremost question in the minds of observers of shareholder activism was how the universal proxy card system, now in its second season, had impacted the shareholder activism landscape. The multidimensional nature of shareholder activist campaigns, as well as the imperfect data regarding such campaigns, has tempered the inclinations of market observers to make definitive claims about its effect. Observers have noted that the 2024 proxy season saw a similar number of public campaigns as compared to previous years. However, activists had significantly more difficulty in 2024 electing directors at the ballot box. Definitive answers about the effect of universal proxy are elusive, given that much activism occurs out of public view and that companies may have a decreased willingness to permit weaker campaigns to proceed to a shareholder vote.

Meanwhile, shareholder activism is still a staggeringly prevalent phenomenon in the U.S. markets, and yet it does not necessarily bring benefit to all

companies and the broader spectrum of shareholders. In this context, the universal proxy card still provides leverage in the hands of activists. Public companies should be well prepared in advance for shareholder activism generally. Specifically, they should prepare to strategically manage and leverage the universal proxy card in the event they find themselves headed toward a proxy contest.

SHAREHOLDER ACTIVISM AS AN ENDURING FEATURE OF THE CORPORATE LANDSCAPE

To appreciate the role of the universal proxy card in today's landscape, it is important to step back and take note of the prevalence of shareholder activism. Since 2022, approximately 1,000 public campaigns have been initiated at companies traded on U.S. exchanges.¹ If

¹ Based on DealPoint data for activism campaigns initiated from 2022 to August 30, 2024 for corporations traded on U.S. exchanges and OTC markets. Excludes closed-end funds.

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private campaigns were included, the number would be substantially higher. Considering that there are roughly 4,000 companies traded on the U.S. national exchanges, this number of public campaigns in two and a half years itself speaks to the high levels of shareholder activism in the U.S. market.²

The majority of activist campaigns take place at small cap and microcap companies, where activists need less money to take significant positions, and may have a greater ability to take management by surprise. Since 2022, about 75% of campaigns have occurred at companies with market capitalization under \$2 billion. Only about 17% of campaigns were at midcap companies with market capitalization between \$2 billion and \$10 billion. Meanwhile, there are comparatively few campaigns at the largest companies — even though those campaigns receive the vast majority of media attention. About 10% of campaigns occurred at big cap companies with market capitalization over \$10 billion.

The composition of the field of activists provides a major reason for boards and management teams to be concerned about activist campaigns. A relatively tiny number of activists are the well-known, well-capitalized funds seen routinely on the front pages. Their campaigns are commonly planned far in advance. The escalation of their campaigns is either conducted through surprise “shock and awe” attacks or through long, drawn-out engagements in which boards and management terms are expected to gradually capitulate to the activist’s demands.

Next, a minority fraction of the overall field comprises smaller funds that are full-time or part-time professional activists who initiate a few campaigns a year, some public and some private. Certain of these funds are comparable in their aggressiveness and ability to grasp management attention to the larger funds. Whatever they may lack relatively in size, notoriety, and

advance preparation, they make up for in well-honed tactics, persistence, and connectedness with like-minded investors throughout the market. They commonly target smaller companies that are less prepared for an activist approach and have fewer resources to defend against a campaign.

Finally, the rest of the field is composed of significantly smaller funds and entities, along with one-time or occasional activists, that have less well-known track records as activists. Their motives often include a desire to burnish their personal brands, which makes their actions more difficult to predict. At annual meetings since 2022, over 500 campaigns featured a party using activism techniques that launched no other campaign in this window. Only a portion of these parties launched campaigns in prior years.

In this same period, about 25 activist funds initiated or participated in five to nine campaigns each, for approximately 160 campaigns (16% of the data set). These are the professional activists, comprised of a wide range of types of funds, from full-time activist funds with reasonably long track records, as well as relatively amateur activists that target smaller public companies in search of quick results, payouts, or notoriety.³ Any public company needs to take a campaign by one of these professional activists especially seriously.

The overall number of public campaigns remained relatively similar to the few years prior to the universal proxy system. There is no public data on private campaigns, but indications from consistent market rumors are that the number of such campaigns increased. A substantial number of highly qualified directors and officers lost their positions in connection with activism campaigns in 2023 and 2024, in many cases to the detriment of the company.

Against the unpredictable prospects of shareholder activism from a company’s perspective — which activist will strike, what ideas will they offer, and what directors

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Multiple activists approaching the same company in the same proxy season are treated as multiple campaigns.

² Based on Statista data for NYSE and Nasdaq domestic listings.

³ About nine funds initiated more than 10 public campaigns in this period, accounting for approximately 13% of the campaigns in the data set.

will they “recommend” — companies must be vigilant about activism, engage effectively, and learn as much about their activist investors as possible.

With universal proxy in play, many companies appear to be less willing to take campaigns to a vote unless they are confident that the vote outcome will be favorable. Less than 20% of announced campaigns mature into a public proxy fight.

UNIVERSAL PROXY AS A BOON TO ACTIVISTS

Under the universal proxy card rules, which became effective on September 1, 2022, the separate proxy cards issued by a company and dissident shareholder during a proxy contest must include both the company’s and dissident’s nominees. Under this regime, shareholders can give proxy voting instructions on either card in favor of any combination of properly nominated candidates, up to the number of seats for election. Under the previous system, the company and dissident issued proxy cards that included only each party’s proposed nominees. As a result, shareholders were previously unable to “mix and match” their voting instructions for any combination of director candidates from both slates.⁴

Many of the concerns that our practice expressed about the universal proxy system prior to its adoption have been borne out by subsequent experience in the market. In 2021, we provided to the SEC an analysis of its proposed rules for the universal proxy system and specific concerns that we hoped would be addressed.⁵ During that time and after the SEC’s adoption of the final rules, our concerns included that: dissident shareholders would exploit the availability of the universal proxy card, and specifically the uncertainty it creates, as an additional source of leverage when making demands to boards and negotiating with them; dissidents would make aggressive settlement proposals to seek to obtain more seats on boards; shareholders would delegate even more than in the past their proxy voting decisions to the proxy advisory firms, principally Institutional Shareholder Services (“ISS”) and Glass Lewis, which would face practical challenges in determining optimal voting recommendations; and special interests and other non-traditional activists could

seek to leverage the universal proxy card to make nominations and launch “single-issue” proxy campaigns (such as in the environmental and social realm of ESG-themed activism).⁶

1. THE SPECTER OF UNCERTAINTY, THE DESIRABILITY OF SETTLEMENT

The universal proxy system has brought added uncertainty to outcomes at the corporate ballot box, and a widely held perception is that it has increased the probability of a partial victory for the activist. This appears to have incentivized companies to settle in lieu of defending a proxy contest.

Companies and shareholder activists have, for a long time, preferred settling with activists to taking fights to the ballot box, but the potential of losing at the ballot box brings particular risk for corporate directors. Since 2022, approximately 200 campaigns were resolved through formal settlement agreements.⁷ During that time period, approximately 75% of board seats obtained by a campaign were obtained through formal settlements. As fiduciaries to all shareholders, including investors with long-term investment interests, directors often feel obligated to prevent a proxy contest in which shareholders may vote with the activist. Some statistical support for this experience may be found in evidence that companies are settling substantially more quickly than in past years.⁸ In numerous campaigns, companies have settled within days of public announcement of their campaigns.

Many activists since 2022 initially sought a control slate or even a “full slate,” only to subsequently settle for one or two seats. These activists leverage the additional uncertainty promoted by the universal proxy regime for potential results at the ballot box. In some cases, activists used a control slate to pressure companies into granting them a settlement for just one director less than control.

⁴ Universal Proxy, SEC Release No. 34-93596 (Nov. 17, 2021), <https://www.sec.gov/rules-regulations/2021/11/universal-proxy>.

⁵ Kai Liekefett, Derek Zaba, & Leonard Wood, Sidley Sends Formal Comment Letter on the SEC’s Universal Proxy Proposal, Harvard Law School Forum on Governance, June 18, 2024, <https://corpgov.law.harvard.edu/2021/06/18/sidley-sends-formal-comment-letter-on-the-secs-universal-proxy-proposal/>.

⁶ See, for example, Kai Liekefett, Derek Zaba & Eric S. Goodwin, What The First Universal Proxy Card Contests Say About the Future of Activism, Harvard Law School Forum on Corporate Governance, April 19, 2023, <https://corpgov.law.harvard.edu/2023/04/19/what-the-first-universal-proxy-card-contests-say-about-the-future-of-activism/>.

⁷ See note 1.

⁸ Andrew Freedman, Shareholder Activism by the Numbers, Harvard Law School Forum on Corporate Governance, June 17, 2024, <https://corpgov.law.harvard.edu/2024/06/17/shareholder-activism-by-the-numbers/>.

The prevalence of settlements is a reason to regard cautiously any assessments about the overall state of shareholder activism — particularly as to the relative fortunes of companies versus activists — based on ballot box outcomes alone. In 2023 and 2024 (to August 30), approximately 24 and 19 proxy contests went to a final vote, respectively.⁹ This is a small sample from which to extrapolate generalizations. Bespoke factors in campaigns undermine the ability to generalize. There are sometimes contests where a company has superior information to the activist that confers a decisive advantage; there are contests where an activist is fighting to make a name for itself and will “fight to the death,” regardless of its low probability of success; and there are many contests where the final result comes down to the vote of one investor, whose preferences are difficult to predict.

2. NEW ACTIVISTS, OCCASIONAL ACTIVISTS

The proxy seasons of 2023 and 2024 have seen a significant influx of first-time activists or activists with little to no track records. According to Lazard data, 2023 saw a record number of first-time activists initiating campaigns.¹⁰ Additional market research found that a third of activist campaigns in 2023 were launched by first-time activists.¹¹ Still, other data shows that since 2022, approximately 50% of announced campaigns featured a fund that has launched no other campaign in this window, while only a portion of these activists launched campaigns in prior years.¹² In our own experience in the last two years, we have seen multiple instances where a new or relatively new activist claimed during negotiations with management or the board that the universal proxy card had encouraged the shareholder to enter the activist fray.

As noted, the majority of activist campaigns occur at smaller companies, where it is easier for a fund or another activist party to obtain a toehold stake or use a de minimis share position as a bully pulpit. The market also has its fair share of “shakedown artists,” or activists

who hold relatively few shares of stock and then use the threat of running a proxy contest with the universal proxy card to extract a settlement from the company. One of the notable players in this space has run 12 campaigns in the past few years.

3. COMPLEXITY AND EXPENSE

The universal proxy card has facilitated new types of complexity in corporate elections. It created the playing field for the novel break-out of a three-way contest at Disney, pitting three slates against each other. How this contest benefited shareholders will remain a matter of discussion. The incumbent directors remained in place, and the company reported estimated proxy solicitation expenditures (above ordinary proxy solicitation costs) of \$40 million, the highest estimated cost for a company’s proxy solicitation in an election contest in 10 years.

In terms of estimated cost, three other high-cost contests have occurred in the new universal proxy era: Icahn vs. Illumina (estimated \$31.5 million), Strategic Organizing Center vs. Starbucks (estimated \$21.9 million), on which more below, and Ancora Advisors vs. Norfolk Southern (estimated \$17.5 million). DealBook, reporting on the contest and having interviewed participants and advisors, found it obvious that “new proxy voting rules changed the fight’s dynamics” by allowing “shareholders to more easily vote for a mix of candidates” from multiple sides.¹³

4. PERSONALIZED CONTESTS

The universal proxy system has shifted the focus away from company versus dissident slates (i.e., a “slate contest”) and toward pitting an activist’s best individual nominees against the company’s individual nominees whom the activist regards as the weakest targets (i.e., a “candidate contest”). Contests may have greater focus on competing director candidates and their qualifications than on competing ideas between the company and dissident as to the direction of the company. This is especially seen in activism outside of large- and mega-cap companies. This can make it even more difficult for companies to predict outcomes of an activism campaign with a relative degree of comfort during the earlier phases of engagement (many months before the annual meeting), as dissidents will often not disclose their director candidates to a company until the annual meeting is only two to three months out.

⁹ See note 1.

¹⁰ Activist Investors Enjoy Strong Rebound in '23, Gird for More Proxy Fights, Reuters, Jan. 16, 2024, <https://www.reuters.com/business/finance/activist-investors-enjoy-strong-rebound-23-gird-more-proxy-fights-2024-01-16/>.

¹¹ Shareholder Activism and the 2024 Proxy Season, Tapestry Networks, May 2024, <https://www.tapestrynetworks.com/wp-content/uploads/2024/06/May-2024-CTGN-Summary-of-Themes.pdf>; Barclays, May 16, 2024.

¹² See note 1.

¹³ The Takeaways From Disney’s Board Fight with Nelson Peltz, DealBook, Apr. 4, 2024, <https://www.nytimes.com/2024/04/04/business/disney-iger-peltz-proxy-battle.html>.

Universal proxy has also made proxy fights more personal, causing activists and companies to dig further into the track records and experience of individual director candidates rather than focusing more on quality of overall slates. When reviewing the Disney proxy fight, DealBook observed this impact of the universal proxy card here as well, finding that as “each side was fighting against specific individuals, instead of against an entire slate, attacks became more personal.”¹⁴

The prospect of a personalized proxy contest further pressures incumbent nominees to settle; this also has incentivized activists to step up individualized attacks on directors. To some extent, a director who joins the board of a visible, mega-cap company may reasonably anticipate the possibility of public exposure and public criticism, even where unwarranted. But more activism occurs at smaller companies with directors who may have less in the way of such expectations. In more than one campaign in 2024, companies and activists vigorously criticized the track records of director candidates from the opposing side in a manner that would not have occurred prior to the advent of the universal proxy.

As a result of the increased uncertainty and complexity under the universal proxy system, shareholders can wind up delegating proxy voting decisions to proxy advisory firms even more than they did before the new rules became effective. One could surmise that this challenge would be mitigated by ISS and Glass Lewis focusing their resources and attention on the individual qualifications of directors, all the more to discern the optimal voting combination in election contest. However, the hope of optimized recommendations is elusive considering how often their voting recommendations on director candidates differ.

In the era of universal proxy, ISS has recommended for a single dissident candidate more commonly than in the three years before the current era (excluding the pandemic-impacted 2020 proxy season). It is uncertain whether this trend reflects a greater willingness of ISS to recommend in favor of one dissident nominee in situations where ISS might have previously recommended for multiple nominees, or in situations where it would have previously recommended for none. It will also take additional years to see if this trend continues for proxy fights featuring two or more dissidents. For the time being, this trend gives additional leverage to dissidents who would launch a proxy contest with the minimal objective of placing at least one director on the board.

5. THE PROXY ADVISORS AND THE LARGEST INSTITUTIONAL INVESTORS

In the era of universal proxy, ISS and to a lesser extent, Glass Lewis, have set the outer bounds for how many, and which, dissident director candidates, if any, will be supported by the top three institutional investors.

From our perspective, it would appear that the personalized contest system puts additional pressure on ISS and Glass Lewis to understand each of the director candidates individually and how each fits into the integrated whole of a board’s functionality. Companies and activists know from experience in contested elections that each side is only able to spend limited time with ISS in a face-to-face meeting, and they may or may not be invited to spend time with Glass Lewis. In this one meeting, a company needs to walk through its campaign thesis, address the dissident’s thesis, explain the finer but vital details of the company’s business (which the activist’s campaign may fail to appreciate), answer many pointed questions of the proxy advisor, and then, finally, if there is time, address the specifics of why the company’s candidates are better than the dissident’s candidates. Little time remains for careful discussion about the individual director candidates, even if this is among the most important topics in the contest.

Comparable constraints apply with respect to the largest institutional investors who make voting decisions independently of (even if partly informed by) the proxy advisory firms. Major institutional investors are forced to make consequential voting decisions about the capabilities of director candidates based mainly on a paper record put out by each side in a contest, and in some cases, a discussion with certain individual director candidates where each candidate may speak for only a few minutes. Such a system overemphasizes a nominee’s ability to speak articulately for a short time at the cost of other beneficial attributes that are not observable in a short conversation. Activist investors, who understand this system, search for their nominees accordingly.

6. A BOON TO ESG-THEMED ACTIVISM

The universal proxy era has also witnessed the emergence of breakthrough developments for activism campaigns wielding an ESG campaign theme. One of the first indications this could happen came when ISS issued a research note on the new universal proxy cards and detailed what would be its approach to ESG-themed director campaigns.¹⁵ ISS noted that its framework for

¹⁴ *Id.*

¹⁵ Kai Liekefett, Derek Zaba & Leonard Wood, ISS Provides Guidance on the Universal Proxy Card, Harvard Law School

evaluating competing positions in a proxy contest favors activist campaigns that “connect the dots between ESG issues, operational concerns, and shareholder value.” This observation outlined a roadmap for activists to effectively leverage ESG themes to bolster activist campaigns otherwise focused on traditional economic bases.

Next in line, one of the most prolific supporters of ESG-focused shareholder proposals, who has filed thousands of shareholder proposals at corporations under Rule 14a-8, began organizing panels and making other public announcements about the potential of using the universal proxy card to advance environmental and social priorities agenda through director elections.¹⁶ In various online discussions and blog posts, this prolific shareholder proposal proponent picked out specific mega-cap company targets and contemplated a strategy for moving beyond Rule 14a-8 proposals, opining, “We need to move beyond filing 20+ proposals We need board candidates who share our concerns and anticipate, rather than just react to issues as they arise.”¹⁷

The 2024 proxy season then saw the blockbuster event of the Strategic Organizing Center (“SRO”), a first-time activist, which launched a proxy contest at Starbucks to elect three dissident directors in support of worker rights. SRO is a long-time coalition of three unions: SEIU (Service Employees International Union), CWA (Communications Workers of America Union), and UFW (United Farm Workers). SEIU led several union organizing efforts at the company in recent years. The campaign began in November 2023 and went almost all the way to the ballot box in March 2024. Even when the board appointed three of its own self-sourced director candidates to the board in January, the activist

group was undeterred.

While the SRO owned a mere 162 shares, the company made two dozen SEC filings in support of its defensive proxy campaign and estimated that its proxy solicitation costs would ultimately be \$21.9 million — one of the highest estimated values for a company’s defensive solicitation ever disclosed. Although the SRO did not win board seats, the campaign was viewed as a success by many observers because the company committed to reengage in labor negotiations with the unions.

SRO’s campaign may be a test run for ESG campaigns through universal proxy, as the campaign established a roadmap for similar undertakings at other companies. SRO estimated spending \$3 million on its campaign — no shoestring budget, but also nothing close to Starbucks’ expenses nor what would have been required prior to the universal proxy era. It engaged a team of top-notch outside advisors known for their work for activist funds. Previously, SRO would have needed to spend additional money mailing its proxy card to shareholders (which is typically done more than once) rather than relying heavily on the company’s distribution of its own proxy card.

It says little that these ESG campaigns are currently limited and that investors holding the majority of stock were unsupportive of SRO’s campaign. The campaign succeeded in bringing attention to the SRO’s cause. Just a few years ago, certain shareholder proposals under Rule 14a-8 on ESG topics that were considered fringe were also infrequent and received no support from proxy advisors. Today, many of those proposals are commonplace, if not regarded as tame, and support from ISS or Glass Lewis is assured on many of these proposals, regardless of the company’s case.

RECOMMENDATIONS FOR PUBLIC COMPANIES

In the era of universal proxy, our advice to public companies remains much as it was when the system was first adopted:

Given that activist investors may focus on a board’s most vulnerable directors, boards should have strong procedures to monitor the quality and suitability of directors. Appropriate board evaluation and refreshment processes are a strong defense and may preempt dissident campaigns. Every director should be prepared to articulate why their presence contributes to the effective operation of the board of directors.

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Forum on Corporate Governance, August 29, 2022, <https://corpgov.law.harvard.edu/2022/08/29/iss-provides-guidance-on-the-universal-proxy-card/>.

¹⁶ ESG Via UPC, CorpGov.net, Nov. 8, 2022, <https://www.corpgov.net/2022/11/esg-via-upc-amazon>. See also ESG via Universal Proxy Card, Corporate Accountability Forums, Dec. 21, 2022, <https://www.buzzsprout.com/1947402/11910755>.

¹⁷ *Id.* See also ESG Proposal or Director Nomination? The Activist Investor (Michael R. Levin), <https://myemail.constantcontact.com/ESG-Proposal-or-Director-Nomination-.html?soid=1102906894819&aid=QavTyEZTJT4> (“ESG activists should really prefer winning a board of directors seat compared to winning approval of a proposal.”).

Boards should assess incumbent directors with added attention to criteria proxy advisory firms and the largest institutional investors consider important.

These criteria are numerous and include directors' ages and tenure, specific qualifications, diversity of experience, and degree of engagement on the board.

Activist campaigns have become more "personal," and so have companies' defenses of their own candidates. Boards should scrutinize directors' individual biographies — going beyond the simple skills matrix — to conceptualize how directors' strengths and weaknesses on individual and collective bases variously protect them from, and expose them to, activist campaigns.

If faced with a threatened proxy contest, a board should seek expert advice to evaluate potential outcomes of a proxy contest before negotiating with activists. Whether the universal proxy card will give an

activist advantage is a case-by-case analysis best made with the advice of seasoned experts in proxy campaigns.

Companies should consider updating their governance documents to account for the universal proxy rules and to fill other gaps, but do so in a careful manner, and before an activist is running a campaign. Amendments to corporate bylaws can, among other things, require an activist shareholder relying on Rule 14a-19 (the core universal proxy rules) to confirm its compliance with the rule on the company's request and confirm that the company will disregard proxies solicited by the activist shareholder if it fails to comply with the rule. Other amendments are often advisable to ensure a company is adequately prepared for an activism campaign. This is a sensitive task and we recommend making these amendments only with the guidance of highly experienced counsel in this area and with attunement to evolving Delaware case law. ■