

CORPORATE GOVERNANCE FEATURE: ACTIVISM LANDSCAPE CONTINUES TO EVOLVE

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While the number of shareholder activist campaigns in the U.S. remained flat in 2021 compared to 2019 and 2020, going into 2022, companies should anticipate that activism will continue being a powerful lever for certain opportunistic shareholders seeking to extract value and produce “alpha” returns. Specifically, companies should look out for an uptick in activist campaigns focused on ESG issues, and activist campaigns may be launched against “de-SPACed” companies that are underperforming and companies with depressed stock prices.

In addition, we may continue seeing a blurring of the lines between traditional shareholder activism and private equity strategies. Changes in voting strategies at institutional investors could shift the balance in some contests.

ESG: Lessons From ExxonMobil and Shell

ESG activism took center stage, with more ESG shareholder proposals in the first half of 2021 than all of 2020.¹ The most prominent activist event of the 2021 proxy season was the campaign against

ExxonMobil by Engine No. 1, which successfully secured three board seats while only holding a 0.02% stake in the company—a surprisingly low ownership percentage for a successful proxy fight.

This was the first time that ESG issues were key to a contested election, and Engine No. 1's success stemmed in part from the support of passive institutional investors as well as the proxy advisory firms Institutional Shareholder Services (ISS) and Glass Lewis, which displayed an increased focus on and support for ESG activism.²

In the coming proxy season, companies should be wary of so-called “Trojan horse” campaigns, where activists combine ESG initiatives with traditional activism campaigns, *e.g.*, a breakup or sale of a company or the nomination of a slate of directors. By pressing both sets of issues, an activist can appeal to the growing concern over ESG factors by institutional investors and, consequently, garner support for their more traditional, non-ESG proposals. A recent example of this is Third Point's campaign against Royal Dutch Shell, where the fund called for the breakup of the oil company into two stand-alone companies, one of which, Third Point argued, could make aggressive investments in renewables and other carbon-reduction technologies.

In anticipation of their 2022 annual meetings and upcoming advance notice windows, companies should conduct a comprehensive review of their ESG policies, posture and disclosures in order to anticipate and respond to any potential threats from activists with an ESG thesis.

2022: The Year of “SPACtivism”?

According to Deal Point Data, in 2021, there were nearly 200 “de-SPACs”—mergers of operating companies into special purpose acquisition companies (“SPACs”). Some of the resulting com-

panies will likely begin seeing a dramatic change in their ownership structures due to expiring lockups for sponsors (typically 12 months) and insiders selling off a portion or all of their shares, some of which may be acquired by activists. With the number of de-SPACed companies in the market, at least some will inevitably underperform, creating an opportunity for activists to put forth a value-creation thesis, whether it be a change in management, sale or breakup of the company, or some other idea.

“SPACTivism” is not limited to de-SPACs. According to SpacResearch, nearly 580 SPACs are currently seeking targets and a combined \$155 billion must be deployed over the next two years. In addition, according to Goldman Sachs, as of September 2021 over 90% of active SPACs were trading below their IPO price. With the deadlines for these SPACs to seek business combinations looming and the Securities and Exchange Commission imposing stricter regulations, SPACs’ stock prices may further decline. That could create an opening for activist investors to buy SPAC shares below their IPO price and exercise redemption rights, forcing a return of the IPO proceeds held in trust at the original IPO price.³

M&A-Related Activism Turns Hostile

According to Lazard’s “Quarterly Review of Shareholder Activism,”⁴ 45% of all activist campaigns in the first three quarters of 2021 had an M&A-related thesis, with activists pushing for a sale or breakup of a company, or the scuttling or sweetening of announced deals.

Activists continue to blur the lines of traditional M&A-related campaigns, pivoting from opposing potential acquisitions and proxy contests to oust board members to launching full-blown hostile takeovers. One example is Carl Icahn’s campaign against Southwest Gas’ proposed acquisition of

Questar Pipeline. That evolved into a contentious proxy contest to replace Southwest’s entire board coupled with a tender offer for all shares of the company.

In addition, 2021 saw the final chapter of the CoreLogic situation, which ended in a sale of the real estate data company to Stone Point Capital and Insight Partners. It began in 2020 when Senator Investment Group teamed up with Cannae Holdings, a strategic buyer, on an unsolicited proposal to acquire CoreLogic. After their proposal was rejected, they persuaded shareholders to elect three new directors to the CoreLogic board.

Throughout 2022, companies can expect more activists to pursue private equity-like strategies. When an activist shareholder threatens to launch an M&A-related campaign, companies should establish a clear strategy for responding if the activist aims to buy the company.

Universal Proxy Cards May Facilitate Shareholder Activism

On November 17, 2021, the SEC voted to adopt new rules requiring companies (other than registered investment companies) to include all nominees (*i.e.*, both company and dissident nominees) on a universal proxy card for contested director elections, effective for all relevant shareholder meetings held after August 31, 2022.⁵

Traditionally, during a contested election, shareholders who were not voting in person had to choose between the company’s and the challenger’s proxy cards, with their competing slates of directors. The SEC’s new “a la carte” rule may make it easier for dissident shareholders to obtain board representation by allowing shareholders to select nominees from both slates on the same proxy card.

It remains to be seen whether the universal proxy

card will result in an uptick in contested elections. But companies will need to consider the potential shifts in how activists approach contested elections, including with regard to the number of candidates they propose and how they communicate their preferred candidates. Companies will also have to consider the impact of a “split decision” by ISS and Glass Lewis, which would make election outcomes more difficult to predict.

Shifting Voting Trends at Index Funds

BlackRock announced that, beginning in 2022, it will give its largest investors (*e.g.*, pension funds and endowments) the ability to cast votes tied to their investments on matters including board seats, ESG proposals and “say on pay.”

If other large index fund firms follow suit, it would result in a shift in voting power from the passive index funds to their larger investors, and would likely cause shareholder proposals and contested election outcomes to be less predictable. It could also become harder for companies to influence the voting decision-makers and to predict how large blocks of shares will be voted. In order to mitigate such volatility, companies will need clear and concise business strategies and robust communication and shareholder engagement plans in advance of the coming 2022 proxy season and going forward.⁶

ENDNOTES:

¹See “Investors Press for Progress on ESG Matters, and SEC Prepares To Join the Fray,” <https://www.skadden.com/insights/publications/2022/01/2022-insights/corporate/investors-press-for-progress>.

²See “What the Exxon Mobil Shareholder Votes Mean,” <https://www.skadden.com/insights/publications/2021/06/the-informed-board/what-the-exxon-mobil-shareholder-votes-mean>.

³See “Choppy Market for SPACs and PIPEs, Competition for Targets Spurs Deal Innovations,” <https://www.skadden.com/insights/publications/2022/01/2022-insights/corporate/choppy-market-for-spacs-and-pipes>.

⁴ <https://www.lazard.com/perspective/lazards-quarterly-review-of-shareholder-activism-q3-2021/>.

⁵See “SEC Mandates Universal Proxy Cards in Election Contests,” <https://www.skadden.com/insights/publications/2021/11/sec-mandates-universal-proxy-cards-in-election-contests>.

⁶See “Institutional Investors, Activists and Legal Reforms Begin Altering Japanese Corporate Governance,” <https://www.skadden.com/insights/publications/2022/01/2022-insights/corporate/institutional-investors-activists-and-legal-reforms>.