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ADVISORY PRACTICE

ESG & Proxy Contests: ESG Themes in 2022 Shareholder Activism Campaigns

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After the 2021 landmark victory by Engine No. 1 at ExxonMobil where a newly-formed activist hedge fund won three board seats using primarily ESG themes in its campaign, many observers believed that 2022 would see a wave of ESG-themed proxy contests for board representation. Two of the most notable ESG-focused activism campaigns in 2022 involved Carl Icahn at McDonald's and Kroger where he focused on animal welfare issues. After receiving less than 2% of the vote on his director candidates at McDonald's, Icahn withdrew his campaign at Kroger commenting that "[i]t is clear that shareholders, even if they are concerned about the issues we highlighted, are not willing to change the board configuration if a company is performing well financially".

While the 2022 proxy season did not have an ExxonMobil-type proxy contest and saw Icahn defeated, activists frequently used ESG themes in campaigns. The ESG issues they raised often resonated with investors even if they were not outcome determinative. Companies should review their ESG profile with shareholder activism in mind as ESG deficiencies can create significant vulnerabilities in defending against an activism campaign.

Examples of activist shareholders using ESG in activism campaigns in 2022 include the following:

- **Huntsman Corporation / Starboard Value:** Starboard criticized Huntsman for having the worst ESG rating among its peers, lacking rigor and vision in its environmental goals, and not providing investors or employees a fulsome view into the company's current workforce composition or practices.
- **Guess?, Inc. / Legion Partners:** Legion argued that improved conditions for Guess? models and employees would represent significant and lasting ESG improvements and urged Guess? to form an ESG committee.
- **Shell plc / Third Point:** Third Point indicated that Shell should be divided into multiple companies, including a legacy energy business and a separate liquified natural gas, renewables, and marketing business, arguing that this would likely lead to an acceleration of CO2 reduction, as well as increased shareholder returns.
- **Kohl's Corporation / Macellum Capital Management:** Macellum noted that despite all of Kohl's ESG claims it incurred a significant penalty for greenwashing by the Federal Trade Commission.
- **Southwest Gas Holdings, Inc. / Carl Icahn:** Icahn argued that Southwest Gas' statement indicating that the acquisition of Questar Pipelines accelerates its energy transition strategy by strengthening its ability to provide affordable low carbon energy to customers was largely greenwashing.
- **SSE plc / Elliott Management:** Elliott argued that SSE should spin off its renewable energy business and enhance corporate governance by adding renewables expertise to the board, among other initiatives, which would allow SSE to establish its leadership position as the U.K.'s renewable energy champion.

The importance of ESG in proxy contests is likely to become even more magnified given that the SEC's universal proxy rules take effect September 1, 2022. Under the universal proxy rules, an activist's nominees are now required to be included on the company's proxy card provided the activist meets certain minimum solicitation and timing requirements. Universal proxy will likely lead to an increase in proxy contests due to the increased ability of an activist to get at least one or two seats on a board. It also may cause E&S activists, governance activists, smaller investment funds, individuals, and so-called corporate gadflies to run proxy contests where they seek both board representation and submit multiple shareholder proposals pursuant to a company's advance notice provisions. While the universal proxy rules do not apply to shareholder proposals, from a practical perspective, it will be difficult for companies to exclude proposals contained in an advance notice from their proxy card in a proxy contest due to their inability to exercise discretionary authority to vote on a shareholder proposal if the activist shareholder satisfies the requirements of Rule 14a-4(c) of the Securities Exchange Act of 1934.

