



*The American Consumer Institute*

***Shareholder Engagement,  
ESG, and the Drift Toward  
Shareholder Activism***

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# Shareholder Engagement, ESG, and the Drift Toward Shareholder Activism

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Shareholder proposals present the opportunity for stakeholders to weigh in on company issues. Historically, shareholder proposals were few in number and centered on corporate governance. However, proposal submissions have increased over the last few decades, and the focus has shifted toward social and environmental issues. In addition, a large portion are submitted by the same small handful of individuals who often resubmit the same proposals across multiple years. This creates a heavy burden on businesses that are forced to expend resources to consider proposals outside the scope of their operations; this could result in diminished profits and a hit in stock prices or impact consumers through increased prices on goods and services. To address the ongoing problems facing the proposal process, this report looks at the history of shareholder activism, how it has evolved, and potential policy solutions to reduce the unnecessary burden on businesses.

## History and Purpose of Securities and Exchange Commission

The Securities and Exchange Commission (SEC) was formed in 1934 with the purpose of “protecting investors; maintaining fair, orderly, and efficient markets; and facilitating capital formation.”<sup>1</sup>

Rule 14a-8, adopted in 1942, provides a framework that allows public-company shareholders to present their own proposals at shareholder meetings, giving all shareholders the ability to vote on such proposals. The provisions also allow for a company to exclude proposals within certain parameters.

In 1945, the SEC released a statement from the Division of Corporation Finance clarifying the scope of rule 14a-8 (at the time, Rule X-14A-7):

*It is the purpose of Rule X-14A-7 [for stockholders] to bring before their fellow stockholders matters of concern to them as stockholders; that is, such matters relating to the affairs of the company concerned as are proper subjects for stockholders' action under the laws of the state under which it is organized. It*

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<sup>1</sup> “About the SEC,” U.S. Securities and Exchange Commission, webpage downloaded December 18, 2023, <https://www.sec.gov/about>.

*was not the intent of Rule X-14A-7 to permit stockholders to obtain the consensus of other stockholders with respect to matters which are of a general political, social or economic nature. Other forums exist for the presentation of such views.*<sup>2</sup>

In 1952, and later with amended language in 1972, the SEC codified its earlier interpretation on topics that were not appropriate for shareholder proposals. Such proposals included those that request or mandate that action be taken toward a general economic, political, racial, religious, or social cause that is not significantly related to or within the control of the business.<sup>3</sup>

In recent years, however, the SEC updated its interpretation of these rules in ways that narrow companies' ability to exclude proposals, effectively facilitating shareholder activism. The SEC's rule places the burden on the company to convince the SEC staff that the proposal is improper and can therefore be excluded from the company's proxy statement. The company must convince the SEC through the no-action letter process that the proposal does not meet procedural or substantive provisions.

Additionally, in 2020 the SEC updated its resubmission and ownership requirements raising the threshold for submitting proposals. If a shareholder wishes to submit a proposal to a given company, that individual must demonstrate stock ownership in one of three ways:

- a) At least \$2,000 in market value of the company's securities for at least three years (an increase from 1998's \$1,000);
- b) At least \$15,000 in market value of the company's securities for at least two years; or
- c) At least \$25,000 in market value of the company's securities for at least one year.

Proposals can be resubmitted year after year, as long as they meet the following requirements: the proposal would need to have earned a vote of five percent support in its first year, 15 percent in the second year, and at least 25 percent in year three.

A proposal can result in a negotiated withdrawal in exchange for action by the company. If agreement is not reached, the resolution is placed on the company's proxy statement and voted on by all stockholders. A proposal doesn't need a majority vote to garner attention. Even 10 to 20 percent approval would often be difficult for a company to ignore, perhaps placing pressure on management to respond. Those who submit count on this.

Some individuals view proposals as a powerful way to influence corporate behavior, steering it in a way that they deem favorable. This activism, combined with recent interpretations at the SEC, has created a problem for businesses.

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<sup>2</sup> See Securities and Exchange Commission, Shareholder Proposals: Staff Legal Bulletin No. 14L (CF), available at: <https://www.sec.gov/corpfin/staff-legal-bulletin-14l-shareholder-proposals>.

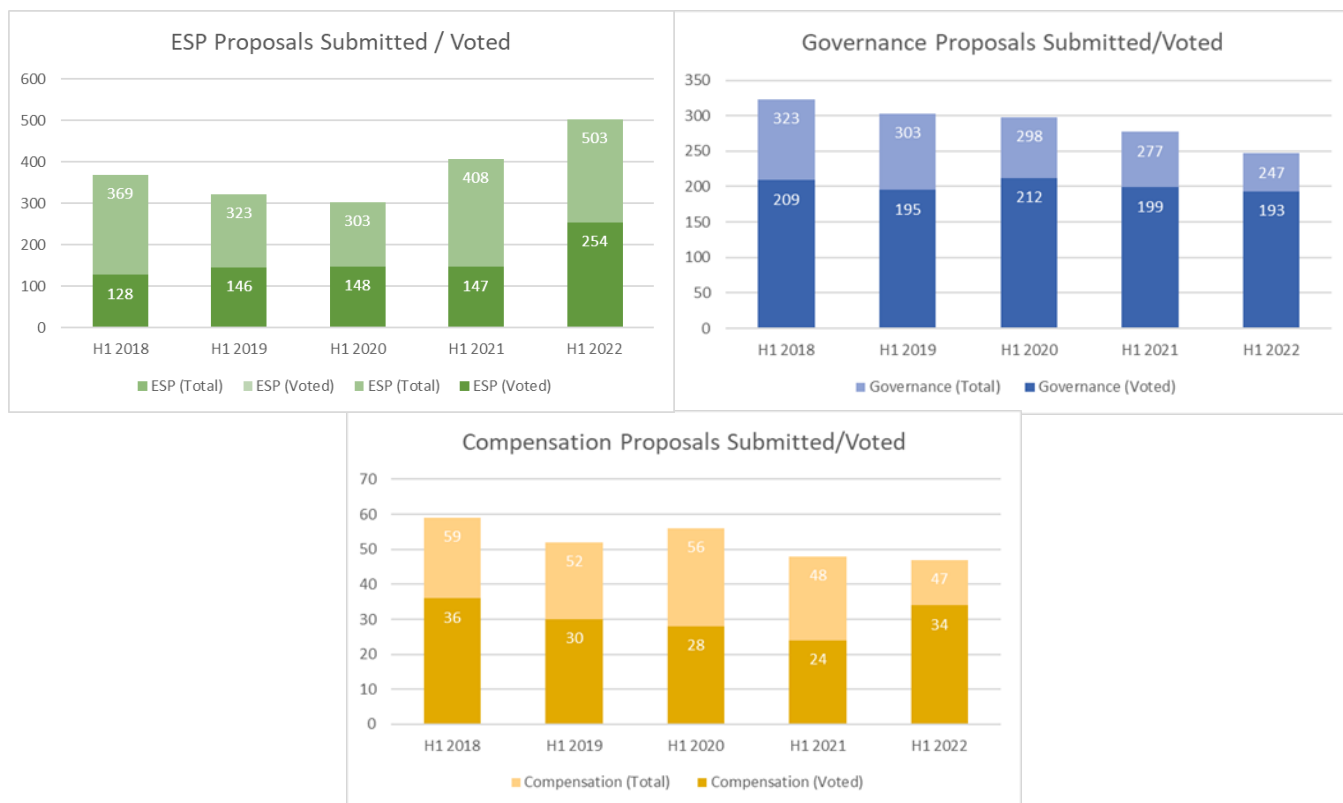
<sup>3</sup> Jill Fisch, "From Legitimacy to Logic: Reconstructing Proxy Regulation," University of Pennsylvania, Carey Law School, 1993, [https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2288&context=faculty\\_scholarship](https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2288&context=faculty_scholarship).

## Rule Changes and Environmental Social Governance

On November 3, 2021, the SEC, under Chair Gensler, published Staff Legal Bulletin 14L, which rescinded interpretations issued under previous chairs by now allowing proposals that “raise issues of broad social or ethical concern related to the company’s business.” Beyond micromanaging, companies will now have more difficulty excluding proposals, specifically those related to Environmental Social Governance (ESG).

ESG hit the scene in the early 2000s and started making it to boardrooms and shareholder proposals within the decade. The last several years, however, have not only seen an increase in the number of overall proposals submitted but a significant uptick in the number associated with ESG policy. Figure 1 illustrates the trends among the various submission categories of S&P 1500 companies, with a noticeably sharp increase in environmental/political topics (ESP) in just the last few years.

Figure 1

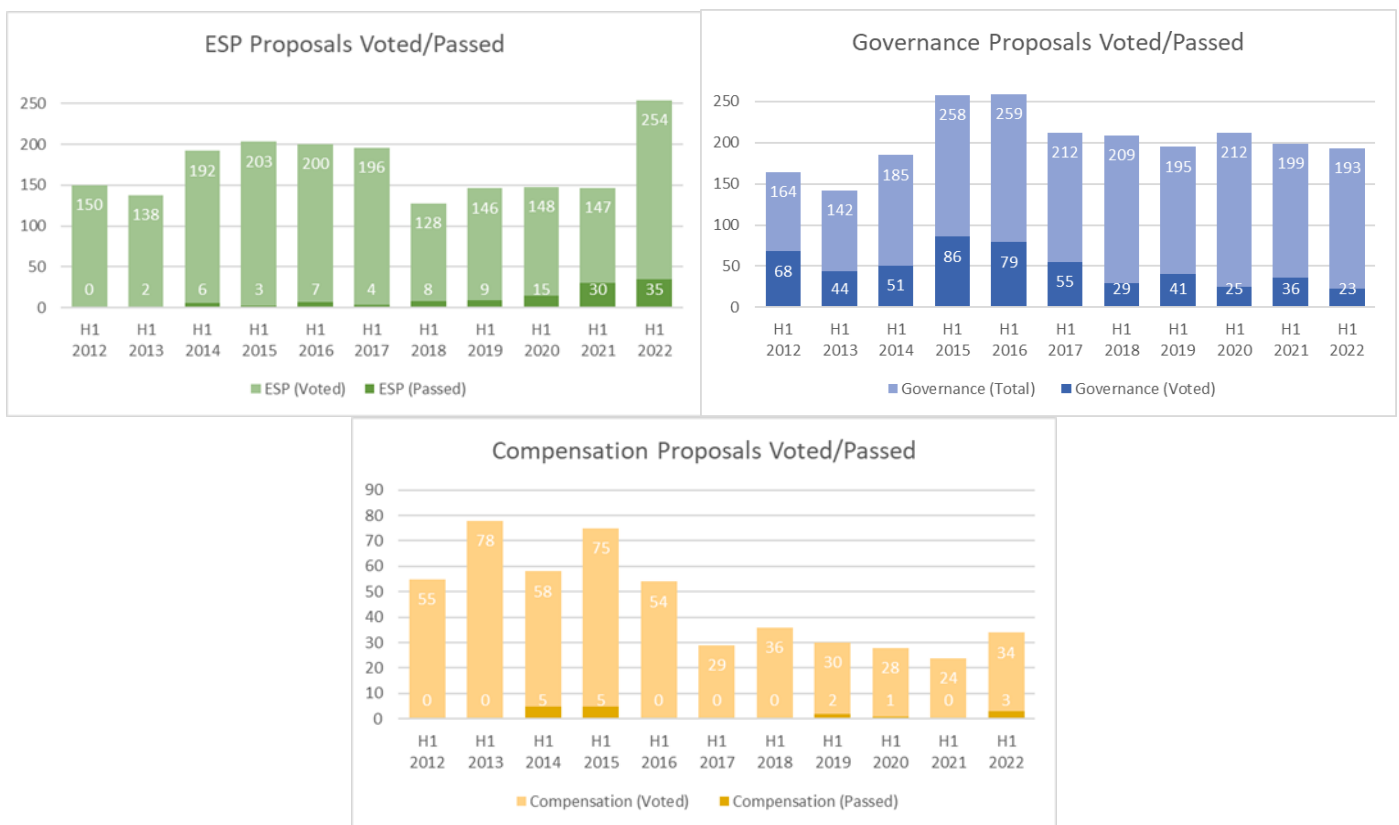


Data from Harvard Law School Forum on Corporate Governance<sup>4</sup>

<sup>4</sup> June Hu, Melissa Sawyer, and Marc Travino, “2022 Proxy Season Review: Rule 14a-8 Shareholder Proposals,” *Harvard Law School Forum on Corporate Governance*, August 25, 2022, <https://corpgov.law.harvard.edu/2022/08/25/2022-proxy-season-review-rule-14a-8-shareholder-proposals/>.

S&P 1500 companies are now receiving more proposals than ever, and a large portion is ESP-related. Specifically, the year 2021 saw a record-breaking number of proposals totaling 733, followed by 797 submissions in 2022. An incredible 503 of those were ESP and put on the proxy statement to be considered by the board compared to 220 just a decade ago. Yet, the number of governance-proposed submissions related to business operations is relatively unchanged. Proposals on ESP now represent a much larger portion of total submissions, surging to 63 percent. And, for the first time, likely due to support from SEC changes, more than half of ESP-related submissions reached a vote in 2022.

Figure 2



Data from Harvard Law School Forum on Corporate Governance<sup>5</sup>

The total number of proposals reaching a vote has increased dramatically under the current Gensler SEC, with fewer proposals being excluded through the no-action process. Yet, the number of proposals that shareholders support is relatively low and declining, suggesting

<sup>5</sup> June Hu, Melissa Sawyer, and Marc Travino, 2022.

that the SEC is requiring votes on irrelevant proposals. Interestingly, the governance proposals reaching a majority vote have seen a dramatic decline, while the ESP proposals are experiencing a gradual increase in passage.

### **Frequent Flyers, AKA “Corporate Gadflies”**

There are groups and individuals who submit proposals to a multitude of organizations year after year. The technical name for these is *corporate gadflies*. Gadflies are tiny insects that bite and annoy livestock. Greek philosopher Socrates once referenced himself as a gadfly who goes around “irritating people so as to make them think, and to reconsider their arguments.”<sup>6</sup> Now, the corporate gadfly is a pesky shareholder who submits massive numbers of shareholder proposals.

The late Evelyn Davis, who became a millionaire through four divorce settlements and the investment of her father’s money, owned stock in at least 80 public companies. Relishing her self-appointed title “Queen of the Corporate Jungle,” Evelyn spent decades shaking up annual meetings.<sup>7</sup> She reportedly sold her annual newsletter “Highlights and Lowlights” to the same CEOs she badgered, charging approximately \$600 a copy. Most bought the two copies she pushed on them, likely to stay in her good graces. But of the 148 proposals she submitted to Fortune 200 companies over her lifetime, only one was approved by a majority of shareholders.<sup>8</sup>

This generation’s crop of gadflies consists of a small group who have their hands in a number of “cookie jars” presumably for the sole purpose of submitting proposals. John Chevedden holds stock in 80 companies and files approximately 100 shareholder proposals a year, with a lifetime achievement of more than 1,000 proposals.<sup>9</sup> Historically submitting on corporate governance, he has recently shifted to social priorities. James McRitchie and his wife, Myra Young, have also submitted hundreds of proposals. They hold stock in 200 companies and submitted 80 proposals in 2022 alone.<sup>10</sup> The third big player is a father-son duo, William and Kenneth Steiner, where Kenneth has carried the torch for his late father. William was an activist

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<sup>6</sup> “A Political Gadfly,” *New York Times*, May 18, 1936, p. 16.

<sup>7</sup> Evelyn Y. Davis, “Shareholder Activist and CEO foil, dead at 89,” *CBS News*, November 2018, <https://www.cbsnews.com/news/evelyn-y-davis-shareholder-activist-and-ceo-foil-dead-at-89/>.

<sup>8</sup> James Copland, Yevgeniy Feyman, and Margaret O’Keefe “Proxy Monitor 2012: A Report on Corporate Governance and Shareholder Activism” Manhattan Institute, Fall 2012, p. 9. [https://www.proxymonitor.org/pdf/pmr\\_04.pdf](https://www.proxymonitor.org/pdf/pmr_04.pdf)

<sup>9</sup> Sajin Kishan, “Main Street’s Most Prolific Corporate Agitator Finds a New Battlefield In ESG,” *Bloomberg*, May 2022, <https://www.bloomberg.com/news/articles/2022-05-25/main-street-s-most-prolific-corporate-agitator-finds-new-battlefield-in-esg#xj4y7vzkg>.

<sup>10</sup> Jennifer Williams-Alvarez, “Investors Put Forward More Proposals, Dialing Up Pressure on Companies,” *Wall Street Journal*, August 2, 2022, <https://www.wsj.com/articles/investors-put-forward-more-proposals-dialing-up-pressure-on-companies-11659432601>.

shareholder for over 40 years, devoting about 70 hours a week to the cause.<sup>11</sup> Kenneth averages about 30 proposals a year.<sup>12</sup>

The organization, As You Sow, boasts of being “the nation’s non-profit leader in shareholder advocacy,” claiming that corporations are responsible for most of the pressing social and environmental ills of the day and must be held accountable.<sup>13</sup> With a core mission of promoting environmental and social corporate responsibility, they represent investors across a broad range of ESG issue areas and have used shareholder resolutions since 2010 to “change corporations from the inside out” and “drive companies toward a sustainable future.” The vast majority of their submissions fall into social issue categories, such as climate change, racial justice, diversity and gender equality, political spending, and consumer packaging.

Together, John Chevedden, James McRitchie and his wife Myra, Kenneth Steiner, and the As You Sow nonprofit comprise a sizeable chunk of the total proposals submitted annually to corporations. In 2021, they collectively submitted 345 of the total 733 proposals, which is nearly 50 percent. In 2022, they submitted 334 of the 797 proposals.

The relative ease with which a shareholder proposal can be submitted, and the low cost associated with it, grants individual shareholders powers they usually are not accorded in corporate America.

Corporate gadflies typically suffer little reputational or financial harm by submitting proposals. Rather, they can embrace the stereotype of pesky shareholders and freely submit proposals that might irritate management and the board.

## Proxy Advisory Firms

Proxy advisory firms provide advice and recommendations on how to manage and vote on many of these shareholder proposals. They are supposed to operate independently by conducting research and providing analysis on key issues, helping investors and shareholders make informed decisions.

The two major players in this field are Institutional Shareholder Services, Inc. (ISS) and Glass Lewis & Co. (Glass Lewis). ISS covers approximately 48,000 shareholder meetings in 115 markets, delivering proxy research and vote recommendations while working closely with clients to execute more than 12.8 million ballots representing 5.4 trillion shares.<sup>14</sup> Glass Lewis

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<sup>11</sup> Sana Siwolop, “Shareholder Activist From Basement to Boardroom,” *New York Times*, June 15, 1997, <https://www.nytimes.com/1997/06/15/business/shareholder-activist-from-basement-to-boardroom.html>.

<sup>12</sup> Kenneth Steiner, “Kenneth Steiner Continues Father’s Work,” *Corporate Governance*, May 2020, <https://www.corpgov.net/2020/05/kenneth-steiner-continues-fathers-work/>.

<sup>13</sup> “About Us,” As You Sow, webpage downloaded December 18, 2023, <https://www.asyousow.org/>.

<sup>14</sup> “ISS Governance,” Institutional Shareholder Services, Inc., webpage downloaded December 18, 2023, <https://www.issgovernance.com/about/about-iss/#1570776311994-db534a1e-7bb2>.

covers more than 30,000 meetings each year across approximately 100 global markets.<sup>15</sup> The two of them together control an “astonishing 97 percent of the proxy advisory market.”<sup>16</sup>

Though investors don’t pay much for proxy advisors’ services, these firms have emerged as a major force in shareholder voting. According to a Manhattan Institute study of proxy voting on shareholder proposals, an ISS recommendation in favor of a given shareholder proposal increases the shareholder vote by an average of 15 percentage points. So essentially, a small outfit with 600 employees in Rockville, Md., is influencing 15 percent of the total stock market.<sup>17</sup>

Fifteen percent of the vote may not sound like much, but it does qualify proposals for resubmission under the SEC’s “resubmission threshold” rules. Recall that under current commission guidelines, a shareholder can propose substantively identical proposals on the ballot, year after year, so long as by the third year at least 25 percent of shareholders vote for the proposal.

Proxy advisory firms, in theory, are subject to federal and state laws that not only protect consumers from false or misleading information but require that the advisory firm only consider those factors relating to the economic value of an investment. In practice, proxy firms are not required to disclose their research methodologies, leaving their clients in the dark about how they reached their analysis.

Regulators are similarly ignorant of how to examine proxy advisors’ rationales or even ensure they follow financial laws. Conflicts of interest are also bound to occur. While institutional investors have a fiduciary duty to their clients, the proxy advisory firms that act as a third party do not. Therefore, proxy advisories do not have to act in the best interest of the institutional investors they serve. The firm has no legal obligation to resolve any conflict that may arise.

ESG has crept into proxy advisory firms, and it appears they are ignoring their fiduciary duties to focus more on social preferences. Multiple hearings on Capitol Hill last summer exposed these firms’ commitments that “may interfere with their ability to honor their legal obligations, specifically as they relate to climate and diversity, equity, and inclusion priorities.”<sup>18</sup> Several attorneys general and other experts were called in to testify, and each one disclosed the underlying agenda of these two dominant proxy firms.

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<sup>15</sup> “Company Overview,” Glass Lewis, webpage downloaded December 18, 2023, <https://www.glasslewis.com/company-overview/>.

<sup>16</sup> Thomas Kingsley, “Proxy Advisory Firms, a Primer,” American Action Forum, July 12, 2023, <https://www.americanactionforum.org/insight/proxy-advisory-firms-a-primer-2/>.

<sup>17</sup> James Copland, “SEC needs to rethink its rules on proxy advisory firms,” *Washington Examiner*, July 24, 2014, <https://www.washingtonexaminer.com/sec-needs-to-rethink-its-rules-on-proxy-advisory-firms>.

<sup>18</sup> Sean Reyes, “Statement before the House Committee on Oversight and Accountability,” May 2023, <https://attorneygeneral.utah.gov/wp-content/uploads/2023/05/Reyes-Testimony-FINAL.pdf>.



ISS declares in its own policy guidelines that they will “generally vote against” directors if ISS feels that the company “is not taking the minimum steps needed to understand, assess, and mitigate risks related to climate change” and that financial institutions “have both the power and the responsibility to prompt a global shift away from carbon-intensive activities and . . . must play a central and catalytic role in the global transition to a low-carbon economy.”<sup>19</sup> Glass Lewis bases its recommendations in part on whether a company is adequately pursuing “net zero emissions goals.”<sup>20</sup>

Additionally, ISS recommends votes based on the number of “racially or ethnically diverse members” and a “gender-diverse status.” They would support proposals that require companies to perform “racial equity . . . audits,” particularly if a company has not issued sufficient “public statements related to its racial justice efforts.” Glass Lewis recommends votes based on racial disclosures and the number of gender-diverse directors.

## The Dilemma

The SEC’s interpretation of rules combined with corporate gadflies and proxy advisory firms have created the perfect environment for turning companies’ annual meeting process into a political circus. An unelected federal agency charged with statutory goals of promoting efficient markets and facilitating capital formation shouldn’t be coopting corporate governance structures to have companies driven against their own interests, consumers, and the general interest of investors.

Larger companies have become big targets of shareholder activism, receiving more and more proposals each year. Many of these proposals are increasingly focused on special interests, prioritizing climate change and racial justice over profits and rates of return. A substantial number of resources, both time and money, are spent working through the contents of the proposals, many of which are repeatedly submitted and/or voted down. These costs aren’t necessarily absorbed; they can be passed down to everyone else, including consumers. In addition, this represents an opportunity cost in that these resources are totally wasted and could have been deployed elsewhere for the benefit of both consumers and shareholders.

A very small handful of individuals who own a negligible amount of a company by investing the bare minimum required should not be dictating the company’s direction and priorities. Firms have financial duties, by state and federal law, to maximize returns for their investors. When social activist investors repeatedly foist costs upon companies, these costs are often carried by the vast majority of shareholders who prefer to maximize their return — and who vote against these proposals, time after time. Consumers also bear these costs in the form

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<sup>19</sup> “Proxy Voting Guidelines Benchmark Policy Recommendations,” ISS, December 13, 2021, <https://www.issgovernance.com/file/policy/2022/americas/US-Voting-Guidelines.pdf>.

<sup>20</sup> “Glass Lewis 2022 Policy Guidelines,” Glass Lewis, 2021, <https://www.glasslewis.com/wp-content/uploads/2021/11/ESG-Initiatives-Voting-Guidelines-GL-2022.pdf>.

of higher prices. In short, the average investor and consumer needs protection from these perverse activities.

Similarly, unelected advisory firms should not be utilizing companies for their own experiments of corporate governance. By focusing on racial, gender, and climate ideals they are ignoring their fiduciary responsibilities to maximize their clients' returns to instead enact policies that ought to be carried out by government officials.

The proxy advisory firms recommending ESG investments are utilizing Americans' hard-earned money to further an agenda that no one else signed up for but they themselves want. Studies have shown that ESG-backed funds underperform.<sup>21</sup> This translates to smaller returns for countless Americans who entrust their money to these companies to maximize profits, and it is a violation of a company's obligations.

Proxy firms wield enormous power among shareholders who rely on their recommendations, which may or may not be in the best interest of the company, its shareholders, and society as a whole. These firms are largely unchecked or regulated.

Shareholder advocacy efforts have resulted in an unprecedented paradigm shift in the behavior of company management toward achieving an environmentally and socially sustainable economy. According to the 2022 US SIF Trends report, more than \$18 trillion — nearly \$1 of every \$3 under professional management — now is invested using ESG criteria and community investing strategies.<sup>22</sup>

Essentially, just a small minority of shareholders and a handful of proxy firms are using corporate governance and investment funds to advance their social goals. These goals are not widely adopted and generally would not be enacted through standard democratic procedures.

Overburdening the proposal process with repetitive and even irrelevant subject matter can distract shareholders and executives, forcing them to shift their focus from areas that concern a company's performance and bottom line to those that are inconsequential. It could also reallocate funds that would otherwise be used to expand, reinvest, and/or simply run operations. Companies should be working to run their businesses most effectively by maximizing profits and returns and implementing policies that benefit everyone.

While some recent indicators suggest a slight shift away from ESG-related funding and investments, more must be done to turn the tide away from such harmful tactics.<sup>23</sup>

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<sup>21</sup> Jean-Pierre Aubry, et al., "ESG Investing and Public Pensions: An Update, Center for Retirement Research at Boston College," Number 74, October 2020, <https://crr.bc.edu/wp-content/uploads/2020/10/SLP74.pdf>.

<sup>22</sup> "2022 Report On US Sustainable Investing Trends," United States Sustainable Investment Forum, 2022, <https://www.ussif.org/trends>.

<sup>23</sup> "We're Winning Our War Against ESG Investing," Committee to Unleash Prosperity, October 2023, <https://committeetounleashprosperity.com/hotlines/were-winning-our-war-against-esg-investing/>.

## Recommendations

The policy changes that contributed to an increase in activist shareholders are not due to legislative changes but rather internal rules of the SEC. To solve the issue, Congress should issue legislative guidance to ensure the agency is fulfilling its mission and not unduly burdening companies. Issues for clarification include:

- Clarify that proposals can be excluded if they do not apply to business operations or if they involve general economic, political, racial, religious, or social causes that are not significantly related to or within the control of the business.<sup>24</sup> This could be further strengthened by prohibiting the SEC's ability to include these types of proposals if they relate to general social policy.
- Allow firms to exclude duplicative proposals or proposals that have already been substantially implemented. Consolidating repetitive proposals alleviates the administrative burden on the organization and reduces the incentive to bombard a firm with multiple overlapping proposals.
- Put a limit on the number of proposals a company is required to vote on. This will allow companies to apportion and budget the adequate time and funding needed to manage each year's proposals, assuring that the process does not necessitate an excessive amount of resources. It would also assist in prioritizing the content and issues to be addressed.
- Increase the ownership threshold for filing shareholder proposals to dissuade actions by individuals or organizations not sufficiently invested in the firm. The current thresholds make it relatively easy to meet the ownership requirements that allow shareholders to submit proposals. As a result, the current threshold allows for corporate gadflies to submit proposals while not being meaningfully invested in the company they wish to influence.
- When there are disagreements over proposals that should be included, it should be the burden of the SEC to justify its inclusion. Currently, the "no-action letter" places this burden on the firm to convince the SEC staff that a proposal should be excluded. The SEC should be protecting investors and facilitating fair markets, not creating additional market burdens.
- Reinststitute the 2020 Proxy Advisor Rule, which required proxy advisers to send any research reports to the companies in question at the same time they go to investors. The previous rule also established a way to ensure that investors are made aware of any responses from the companies themselves. This will give companies the chance to react and respond to recommendations before voting takes place.

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<sup>24</sup> Jill Fisch, "From Legitimacy to Logic: Reconstructing Proxy Regulation," University of Pennsylvania, Carey Law School, 1993, [https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2288&context=faculty\\_scholarship](https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2288&context=faculty_scholarship).

## **Conclusion**

The SEC has helped facilitate a climate where individuals and proxy advisory firms can wield their influence on a number of businesses. These proposals, which are often duplicative and/or increasingly social in nature, have placed undue costs on average shareholders they are supposed to protect, and these costs can be passed through to consumers in the form of higher prices on goods and services. While the proposal submission process itself is necessary to raise awareness and promote essential changes, it has unfortunately become a target-rich environment where a select few can push agendas. Neglecting to incorporate any changes to rules and procedures will allow corporate activism to continue to expand and overtake the shareholder proposal process, to the detriment of companies, shareholders, and consumers.