



# Crossing the Wall

Insights from the M&A and Activism  
Communications Team



ARTICLE

## Single Issue Board Candidates: Universal Proxy Creates New Type of Proxy Fight

In American politics there has been a long tradition of candidates for elected office running on a campaign platform defined solely by one issue. These politicians often have a view that simply by running for election it will drive attention to the issue, thus forcing change. This is exactly what happened when the U.S. Securities and Exchange Commission put into effect the Universal Proxy rules this September—it opened the door for single issue candidates in the annual election of board directors. The potential rise of single-issue candidates has important implications for how boards engage with investors, discuss oversight of key issues and protect the reputation of board members.

### Proxy Fights a Mandate for Change

Prior to the universal proxy, traditionally contested director elections were primarily the territory of hedge funds in pursuit of strategic change at the company. An activist investor would focus on persuading shareholders that the company needs to change and all or some of the current board members are not up to the task. Investors voting by proxy were forced to choose either the management card, representing the existing board, or the dissident card, representing the activist's nominees. Winning a proxy contest was as much winning a mandate for change as it was securing the election of new directors.

With the universal proxy, all nominees appear on one slate – even if multiple activists put forth dissident nominees at the same annual general meeting. Investors will now be able to hand-pick their own combination of directors they'd like to elect.

### Universal Proxy Collides with Shareholder Influence Evolution

The adoption of the universal proxy comes at a time when the market is already witnessing an unprecedented level of shareholder influence. Two powerful trends in the market highlight this paradigm shift. First, shareholders now have

the ability to drive favorable proxy outcomes with minimal amounts of investment. The days of needing 5% or more of shares outstanding to have influence are gone. Second, the investors that are pushing companies to change through shareholder proposals or other avenues has never been more prevalent or impassioned. Equally influential is the fact that the universal proxy rules lower the costs of a proxy campaign.

Universal proxy has connected influence, interest and cost in a way that opens the door for more funds to consider putting forth a board candidate for election.

### **Environmental and Social Candidates Likely to Come First**

Now that it is cheaper and easier to run a proxy campaign, it is expected that the first funds to pursue this new method of engagement will be ESG-focused funds or responsible investment funds. If these funds believe a company is an ESG-laggard, they may not simply file a shareholder proposal, but aim to replace (or simply add) directors instead.

An ESG or responsible investment-based proxy campaign would draw significant attention to the company's oversight of the topic and force larger institutional funds with an ESG focus to closely examine the issues. Further, the notion of changing a single director will be easier to sell to other shareholders given the relative influence on the board would remain intact. The goal is not necessarily voting success, rather, the bottom-line value impact is that the fight would almost certainly force change even if it fell short of voting success.

In many ways, Carl Icahn's proxy fight at McDonald's in 2022 is a clear example of the power behind single-issue proxy contests. Green Century Capital Management, a group of shareholder advocates that has seen incredible success with its shareholder proposals, played a prominent role in that campaign – with its president being one of Icahn's nominees. Although the proxy failed in its direct goal of electing directors, however, it was successful in that it drove new, focused attention to critical social issues, particularly those around animal welfare.

The potential creation of single-issue director candidates in a proxy fight changes how activists will approach companies, and thus how boards need to think about activism preparedness. Boards should proactively assess the following to limit activism risk heading into 2023 proxy season:

- **Focus on individual director relevance** – To combat the potential of dispersed votes, activists will have significantly more incentive to spotlight which incumbent nominees should be replaced. This will result in an increase in direct public attacks on individual directors. To mitigate this challenge, boards should focus on strengthening the public narrative on each director's strengths and expertise, and how the board approaches regular refreshment of leadership and perspective.
- **Evaluate director skills against ESG materiality** – Most boards have implemented formal governance oversight of its ESG program, however, many have not evaluated director skills and alignment to the company's stated material ESG issues. Boards should understand and disclose how directors and their relevant committees include pertinent backgrounds on material ESG risks.



- **Know the company's ESG gaps** – A single issue campaign is likely to start with criticism of a discerned weakness in a company's ESG program. Boards should understand how outsiders evaluate their ESG program, how criticisms could resonate with investors and what, if any, deficiencies connect to board oversight concerns.
- **Refresh activism preparation planning** – Most companies have some form of an activism defense plan on the shelf. However, these plans primarily contemplate campaigns from hedge funds seeking to challenge company strategy through board oversight. Boards should update these plans to account for nuances of the universal proxy and how to manage single-issue campaigns.

- **Coordinate shareholder proposals and activism defense** – Shareholder proposals are often treated as a functional legal aspect of the board and proxy statement. That's still primarily true. However, in light of the expanded capabilities of these shareholders to potentially challenge for board seats, it is important that engagement with these investors is coordinated with the broader activism defense planning teams.

Shareholder engagement has unquestionably changed in the time of the Universal Proxy. It can be expected that single-issue candidates will continue to grow and take a strong foothold in setting the strategy for how boards engage with investors. Companies need to be aware of this shift to adequately and meaningfully prepare for this new type of campaign strategy.

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**PAT TUCKER**

Senior Managing Director  
646-578-6877  
pat.tucker@fticonsulting.com

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**GARRETT MUZIKOWSKI**

Director  
202-297-4037  
garrett.muzikowski@fticonsulting.com

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**ALANNA FISHMAN**

Managing Director  
303-689-8828  
alanna.fishman@fticonsulting.com