CORPORATE GOVERNANCE

Shareholder Activism Is the Next Phase of #MeToo

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As the #MeToo movement continues to make itself felt in all facets of American life, public company boards of directors that are newly focused on the issue of workplace harassment have seen corporate responses evolve. In recent months, many boards have overseen the addition of anti-harassment policies to corporate codes of conduct, the establishment of procedures for addressing allegations, and the enhancement of employee training at all levels. Directors are taking proactive steps toward educating themselves and looking deeply into the issues involved, and many have highlighted it as a priority for the senior management team. Boards that have successfully installed the nuts and bolts of good governance in this area can now step back and consider the larger project of gender equality in corporate America, in which sexual harassment, corporate culture, gender pay equity, and gender diversity are related issues. Shareholder activity in all four of these areas—which we will call collectively, "corporate equality"—has markedly increased, and boards looking ahead to the next phase of corporate governance activism should take note of this trend and try to be proactive as opposed to reactive.

Board Accountability for Corporate Culture

Earlier this year, pension fund giant CalPERS revised its corporate governance principles, adding a new policy emphasizing the board's role "in setting a high-performance corporate culture," and urging every public company board to "develop and disclose its efforts towards establishing effective corporate culture, including its anti-harassment policy." The new policy supports disclosure of all settlements, including sexual harassment settlements, involving an executive or

member of the board. CalPERS also added language to its policy on human capital management practices to specifically emphasize the importance of preventing “harassment of any kind including sexual harassment.” CalPERS’s governance policy supporting compensation clawbacks in the event of executive misconduct, and urging corresponding disclosure to shareholders, includes a specific reference to sexual harassment misconduct.

BlackRock, in a statement released in March 2018, elaborated on its approach to human capital management, which it identifies as one of its engagement priorities for the year. Noting that human capital management is an investment issue with meaningful financial impact, BlackRock emphasized that human capital management “is both a board and a management issue.” The statement set forth a list of discussion points on which it intends to engage with boards this year in order to promote board accountability, including the role of the board in overseeing the company’s strategy “to create a healthy culture and prevent unwanted behaviors.” BlackRock’s discussion points also include human capital risk management, diversity in board and workforce composition, and potentially linking human capital management performance metrics to executive compensation.

It has always been the responsibility of the board to set the “tone at the top” for the company and convey the importance of such tone to the senior management team. Effective boards convey their priorities clearly and hold their senior management team accountable. CalPERS’s policy updates and BlackRock’s statement regarding human capital management make clear that powerful shareholders increasingly will hold boards to account for deficiencies in corporate culture that manifest themselves in pervasive harassment, discrimination, lack of workforce diversity, and gender pay inequality.

Shareholder Activism

Trillium Asset Management filed a first-of-its-kind proposal earlier this year at Nike, urging the board to improve its risk oversight with respect to workplace sexual harassment, to focus on its deficiencies in gender diversity and pay disparity, and to produce a report describing its efforts in harassment prevention and creation of a more gender-balanced workforce. The proposal, which also urged Nike to consider company culture and diversity metrics in evaluating the performance of senior executives, was withdrawn upon Nike’s commitment to consider Trillium’s request and to meet quarterly to discuss the results. Trillium also has filed shareholder proposals at numerous companies in the past five years pushing for increased workplace diversity.

The first shareholder proposals regarding sexual harassment online were filed jointly in January 2018 by Arjuna Capital and the New York State Common Retirement Fund. The resolutions at Facebook and Twitter requested that each company produce a detailed report regarding the scope of platform abuses, the efficacy of enforcement of their content policies, and the risks posed by content management controversies. The filers expressed concern that weak anti-harassment policies and minimal enforcement create “a threat to women and a danger to long-term shareholder value.”

Arjuna Capital has focused heavily on the gender pay gap in the financial, tech, and consumer retail industries. Six shareholder proposals filed in 2017 at the largest U.S. financial institutions asking for detailed reports on the percentage pay gap between male and female employees were

unsuccessful, but this year, nine out of nine financial institutions targeted—including Citibank, JP Morgan, Bank of America, Wells Fargo, and American Express—have agreed to disclose and close their gender (and in some cases, racial) pay gaps. In July, Arjuna Capital announced that it had engaged 23 companies on the issue of pay equity, including many of the largest tech and retail companies in the United States, and had reached agreement with 21 of them.

As in recent years, 2018 also saw significant shareholder activity relating to gender diversity on boards. Influential investors such as BlackRock, State Street Global Advisors, CalSTRS, and CalPERS have incorporated board diversity into their voting policies, and shareholders have shown a willingness to vote against boards that do not show a commitment to diversity. State Street, for example, has indicated that in the 2018 proxy season it voted against certain directors at more than 500 companies for failure to address board diversity. Chairmen of all-male boards received average opposition votes of over 15 percent this year, as compared to 3.6 percent for the same position at boards with 20 percent female membership. In the S&P 500, 49 percent of boards now have three or more women directors, and for the first time, the rate of increase in board diversity accelerated in 2018.

While relatively few activists have so far been filing the majority of shareholder proposals aimed at corporate equality, that does not mean that it is a fringe movement. The success of Arjuna Capital's 2018 campaign demonstrates the rapidly growing influence of shareholders in pushing companies to adopt socially progressive policies. Activists like Natasha Lamb of Arjuna may be the tip of the spear, but established and powerful shareholders such as CalPERS and BlackRock strongly endorse the connection between corporate equality and long-term value. In contrast to past eras, when it was difficult for activists to gain traction with companies on social issues, and companies were able to exclude or ignore these proposals without public backlash, the cultural context of the current #MeToo movement makes that approach risky and potentially damaging to the company.

In the current climate, public companies have little choice but to engage with shareholders, offer increased disclosure, and work toward developing policies to promote equality in the workplace. Under shareholder pressure, some of the largest and best-known U.S. companies have engaged and acceded to activist demands. The theme of corporate equality has resonance in all aspects of American culture at this moment, and it is on its ascendancy. Boards should take note of this trend and understand that they are increasingly likely to be held accountable for any notable failure to be leaders on this issue—not in the Delaware courts, perhaps, but in the court of public opinion, where a guilty verdict may be unfounded yet still financially significant. It is no small task and will require ongoing attention both to the details of governance as well as to the big picture.

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