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EXIT VS. VOICE: A COMPARISON OF DIVESTMENT AND SHAREHOLDER ENGAGEMENT

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INTRODUCTION

As large corporations have accumulated vast amounts of economic and political power in the past fifty years, citizen activists have shifted from focusing on political institutions to scrutinizing corporate actors. It is telling that Occupy Wall Street, one of the most prominent citizen activist movements of recent years, chose to locate itself physically and metaphorically in the heart of American financial power, not political power. As citizen activist movements have matured, they are becoming more creative in the methods they employ to confront corporate power. No longer content to simply influence corporations by rallying support among the general public, the press, and policymakers, activists are seeking to exert pressure on and through stakeholders in the corporations themselves.

Activists have turned their attention to the actual owners of the corporations: the shareholders. Recognizing that shareholders occupy a hallowed position in the hierarchy of corporate stakeholders, activists seek to enlist shareholders in their causes. It is now commonplace for a well-rounded campaign targeting corporate behavior to woo shareholders to the cause and take advantage of their unique levers of power. These efforts have come to be embodied in two types of shareholder-focused tactics: divestment and shareholder engagement.

While the importance of enlisting shareholders is now well-recognized, the two distinct modes of enlisting their help have not been comprehensively compared with one another. The effectiveness of shareholder engagement versus selling shares has been discussed extensively in the context of corporate governance and other profit-motivated reforms. And the propriety of the two tactics has been debated in the context of particular social and environmental campaigns.[1] But until now no one has undertaken a thorough comparison of the relative costs and benefits of the two tactics. This Note seeks to address this gap in the discourse by comprehensively analyzing the utility of these two tactics as tools for social and environmental issue activists.

This Note seeks to synthesize insights from social movement research, organization and management studies, economics, corporate law, and activist literature and experiences. The analysis will be largely theoretical but will draw on historical examples from past campaigns to illustrate certain points. Because the analysis of these two tactics requires drawing on a variety of disciplines, each of which warrant individual discussion, this Note is not meant to be exhaustive but rather to provide some useful clarifications and provide a starting point for further discussion.

Part I outlines the rise of anti-corporate activism, introduces anti-corporate activist tactics, describes the various audiences for anti-corporate activism, and explains the Exit and Voice Framework. Part II describes the first tactic, divestment, and refines the focus of the analysis to divestment's consequentialist goals. Part III describes the second tactic, shareholder engagement, discusses its goals and methods, particularly the shareholder resolution, and distinguishes engagement from shareholder activism undertaken for financial or corporate governance goals.

Part IV undertakes to provide a comprehensive analysis of the utility of divestment and engagement. In terms of costs, divestment would not likely reduce an investor's returns but may increase their portfolio risk. Engagement presents more definite costs to pursue the campaign, including monitoring costs. Looking at the efficacy of the tactics, divestment would be unable to inflict direct financial costs on the target unless a critical mass of investable capital divested. Shareholder engagement poses definite costs upon the target in terms of time and money in responding to the effort. More significant than direct financial costs are the expressive effects of the respective tactics. Divestment offers expressive value in the act of disassociation, which is strictly symbolic. Divestment forecloses shareholder engagement and the unique means of communication open to shareholders. Engagement also offers an advantage in terms of the credibility and the types of frames which

1. *See, e.g.*, Fred Small, *Fossil Fuel Divestment Is Moral, Strategic*, UU WORLD (June 3, 2013), http://www.uuworld.org/ideas/articles/285524.shtml; *see also* Tim Brennan, *Fossil Fuel Divestment Is Not the Answer*, UU WORLD (June 3, 2013), http://www.uuworld.org/ideas/articles/285525.shtml.

attach to engagement efforts. Beyond that, engagement offers information-forcing mechanisms. The paradox that a successful divestment campaign may leave a corporation unconstrained also suggests that engagement is the superior tactic.

This Note concludes that shareholder engagement is the superior activist tactic. Engagement offers more powerful messages and means of communication, so it is the stronger expressive mechanism. Engagement should be the preferred tactic, except where the corporation is incapable of reform.

I. BACKGROUND

A. *The Rise of Anti-Corporate Activism*

Citizen activism has traditionally focused on government officials. Movements often target policymakers directly through petitions, letter-writing campaigns, and protests. Citizen activists may also seek to influence media coverage and public opinion in order to indirectly pressure lawmakers. Citizen activism may also focus on corporations in order to influence them to exert pressure on policymakers.

The size and reach of multi-national corporations has increased to unprecedented levels. As of 2014, thirty-seven of the world's one hundred largest economic entities were corporations, not countries.[2] As the scope of operations and scale of corporations has increased, so has their potential to impose negative externalities on society through their practices. Thus their desirability as a direct target for social and environmental activism has increased. The 350.org Fossil Free Campaign illustrates this trend: it seeks to pressure energy companies directly to stop exploring for hydrocarbons and keep eighty percent of their reserves in the ground.[3]

As the wealth, power, and visibility of multi-national corporations has increased, so has their ability to influence governments and the public.[4] Thus their utility as a target for activism derives not just from the impact of their own actions, but also from large corporations' power to influence government policy.[5] This reality informs

2. *State of Power 2014: Exposing the Davos Class*, TRANSNATIONAL INSTITUTE 2014, at 1 (2014), https://www.tni.org/files/download/state_of_power-6feb14.pdf.

3. *Frequently Asked Questions*, FOSSIL FREE, http://gofossilfree.org/frequently-asked-questions/ (last visited Apr. 2, 2016).

4. *See* SARAH A. SOULE, CONTENTION AND CORPORATE SOCIAL RESPONSIBILITY 4 (2009).

5. *See, e.g.*, TORONTO 350.ORG, THE FOSSIL FUEL INDUSTRY AND THE CASE FOR DIVESTMENT 134 (2015), http://www.uoftfacultydivest.com/files/fossil-fuel-divest-

the Boycott, Divest, and Sanctions (BDS) Movement, which seeks to punish and deter companies from doing business with the Israeli military or in the occupied areas of Israel. At least in theory, this tactic creates domestic economic pressure as a means to influence Israeli public opinion and government policy.[6] Directly targeting corporations can be an effective end-run around a recalcitrant national government. Where the U.S. government has proven unwilling or incapable of exerting influence, direct corporate activism can be used to influence the policies of foreign governments. This channeling effect could be seen in the 1970s and 1980s in the effort to end Apartheid in South Africa by exerting pressure on U.S. corporations doing business in South Africa[7] and more recently in the effort to end genocide in Darfur by targeting companies doing business in Sudan.[8]

In the United States, the attractiveness of citizen activism directly targeting corporations has increased relative to that of targeting government policymakers. As money has come to dominate the U.S. political process, the ability of average citizens to influence lawmakers using just the power of their vote has decreased relative to the power of business interests and economic elites.[9] At the same time, *Citizens United* and the rise of Super PACs have made it easier for corporations to spend money on campaigns.[10] Campaign influence and a well-organized corps of lobbyists and think tanks have increased corporations' ability to influence lawmakers to unprecedented levels[11] and have called into question the ability of average citizens to influence policy. Corporations have also proven adept at stymieing and co-opting regulatory agencies charged with monitor-

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new.pdf ("Partly because of the political influence of these corporations—and the effectiveness of their campaign to delay government action—climate change has become an urgent problem.").

6. OMAR BARGHOUTI, BOYCOTT, DIVESTMENT, SANCTIONS: THE GLOBAL STRUGGLE FOR HUMAN RIGHTS 18 (2011).

7. Jennifer Davis et al., *Economic Disengagement and South Africa*: *The Effectiveness and Feasibility of Implementing Sanctions and Divestment*, 15 LAW & POL'Y INT'L BUS. 529, 555–63 (1983).

8. Perry S. Bechky, *Darfur, Divestment, and Dialogue,* 30 U. PA. J. INT'L L. 823, 834–38 (2009).

9. *See* Martin Gilens & Benjamin I. Page, *Testing Theories of American Politics: Elites, Interest Groups, and Average Citizens*, 12 PERSP. ON POL. 564, 576 (2014).

10. *See* US SIF – THE FORUM FOR SUSTAINABLE AND RESPONSIBLE INVESTMENT, CONFRONTING CORPORATE MONEY IN POLITICS, 1–2 (2014).

11. *See* AUGUSTIN LANDIER & VINAY B. NAIR, INVESTING FOR CHANGE: PROFIT FROM RESPONSIBLE INVESTMENT 7 (2009).

ing and limiting the excesses of business activity.[12] Their levers of power include the revolving-door phenomenon and well-coordinated litigation aimed at defeating regulations. In the past, unions and organized labor acted as a potent countervailing force to corporate power. However, union membership and influence has steadily declined over the past three decades.[13] Citizen-activists perceive a lack of oversight over corporations which they seek to fix through direct action.[14]

These concurrent societal trends—the increased scope of activity of large corporations, the concentration of economic and political power in the hands of corporations, and the decrease in countervailing institutional power—have increased the utility of pressuring corporations vis-à-vis lobbying legislators.[15] Another contributing factor is the advent of the Internet and the diffusion of social media technology.[16] The Internet and social media provide a low cost organizing tool and platform for attacking corporate brand identity, leaving corporations increasingly vulnerable to grassroots campaigns.[17]

As the reality of concentration of power in corporate hands has set in, so has an expectation among the general public and an un-

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12. *See, e.g.*, COAL. FOR SENSIBLE SAFEGUARDS, DOWN THE REGULATORY RABBIT HOLE 5–6 (2013), http://www.sensiblesafeguards.org/assets/documents/down-the-regulatory-rabbit-hole.pdf (discussing eight consumer protection efforts that have been frustrated due to industry influence on the rulemaking process as a result of the revolving door phenomenon, the abuse of the judicial review process, and a lack of transparency).

13. *See* Bureau of Int'l Info. Programs, U.S. Dep't of State, Outline of the U.S. Economy 94–95 (Michael J. Friedman et al. eds., 1981 ed. 2012), http://photos.state.gov/libraries/amgov/30145/publications-english/120321_Outline_US_Economy_2012_CX2.pdf.

14. *See* SOULE, *supra* note 4, at 64; *see also* Margaret V. Sach, *Social Proposals Under Rule 14a-8: A Fall-Back Remedy in an Era of Congressional Inaction*, 2 UC IRVINE L. REV. 931, 934 (2012) (discussing the use of shareholder proposals as an alternative means of influencing corporate behavior where "Congress has been unable or unwilling to act"); *see also* Bill McKibben, "Global Warming's Terrifying New Math," ROLLING STONE, July 19, 2012, http://www.rollingstone.com/politics/news/global-warmings-terrifying-new-math-20120719?page=3 (discussing the scientific consensus on the dangers posed by burning more fossil fuels, pointing out the unwillingness of governments to take action, and suggesting that citizens take direct action by divesting from fossil fuel companies).

15. *See* Benjamin J. Richardson, *Are Social Investors Influential?*, 9 EUR. COMPANY L. 133, 138–39 (2012).

16. Natasha Good, *Is Social Media Bad for Business?*, FRESHFIELDS BRUCKHAUS DERINGER, http://www.freshfields.com/en/global/Digital/Social_media_in_the_corporate_sphere/.

17. SOULE, *supra* note 4, at 8. *See also* JAROL B. MANHEIM, TRENDS IN UNION CORPORATE CAMPAIGNS 42–43 (U.S. Chamber of Commerce 2005).

derstanding among business leaders that corporations have a responsibility to act consistently with the interests of the communities in which they operate.[18] This understanding has contributed to the flourishing of the concept of corporate social responsibility (CSR) over the past few decades.[19] Key audiences are receptive to appeals for greater corporate accountability: consumers believe corporations should be more accountable and business leaders understand they need to take more responsibility.[20] As this new reality has set in, we can observe an increase in citizen campaigns that directly target corporations.[21]

B. *Introducing Anti-Corporate Activist Tactics*

1. Audience: Activist Tactics Depend on the Intended Audience.

The most direct tactic for seeking a change in corporate behavior is a general anti-corporate campaign. These campaigns appeal directly to corporate leadership through social media, op-eds, or letter-writing campaigns. They may also seek to influence corporate leadership indirectly by hurting the company's image through leafleting, protests, or disseminating damaging information over the Internet, thereby discouraging people from doing business with the company.[22] An illustrative example of a general anti-corporate campaign would be the Rainforest Action Network's attacks on Mitsubishi for practices leading to the destruction of rainforests.[23] The activists employed traditional tactics like letter-writing and picketing as well as more creative attacks like running full-page ads in the *New York Times* and inflating a large Godzilla balloon at an auto show.[24] The tactics targeted every level of Mitsubishi, from individual retailers to company management to the company's primary

18. MICHAEL HOPKINS, CORPORATE SOCIAL RESPONSIBILITY AND INTERNATIONAL DEVELOPMENT: IS BUSINESS THE SOLUTION? 1–9 (2007).

19. *See, e.g.*, Dirk Matten & Andrew Crane, *Corporate Citizenship: Toward an Extended Theoretical Conceptualization*, 30 ACAD. OF MGMT. REV. 166, 166 (2005).

20. ACCENTURE, THE UN GLOBAL COMPACT-ACCENTURE CEO STUDY ON SUSTAINABILITY 2013, at 11 (2013).

21. Tomás Mac Sheoin, *Transnational Anti-Corporate Campaigns: Fail Often, Fail Better*, 41 SOC. JUST. 198, 200–10 (2015).

22. *See* Trey Kovacs & F. Vincent Vernuccio, *Corporate Campaigns*, COMPETITIVE ENTERPRISE INST. (April 30, 2012), https://cei.org/op-eds-articles/corporate-campaigns (describing public pressure strategy and tactics used by unions against corporations).

23. SOULE, *supra* note 4, at 14.

24. *Id.*

bank.[25] The campaign was ultimately successful in coercing Mitsubishi to engage with the organization and agree to reforms.[26]

Campaigns have also sought to exert pressure indirectly by influencing consumers. Prominent examples of successful consumer-focused campaigns include the consumer boycott of grapes led by the United Farm Workers in the 1960s[27] and the boycott of tuna fish to protest the incidental killing of dolphins in the 1980s.[28] Campaigns may also seek to exert pressure on a company through their suppliers, such as anti-abortion groups pressuring landlords who rent space to clinics where abortions are performed.[29]

Activists have realized that their messages may resonate with company leadership more loudly when they enlist the support of company insiders. Company insiders, as used here, are direct stakeholders with formal relationships with the company and a vested interest in the company's success. For the purposes of this discussion, I will define insiders as the company's employees, management, and shareholders.

In the past fifty years, activists have found a new audience for their messages: shareholders.[30] Shareholders, as the effective owners of the corporation, are an especially attractive audience for activists' messages. In the United States' corporate governance system, the scope of responsibilities owed by corporations to their surrounding communities is ambiguous and controversial, while the responsibility owed to their shareholders is paramount.[31] Activists seek to persuade shareholders to embrace their privileged positions and then take action. For their part, the shareholders may already agree with the activists' positions, and the activists' goals will simply be to educate the shareholders that the company is acting inconsistently with their beliefs. Once a shareholder has decided to

25. *Id.*

26. *Id.*

27. UFW History, United Farm Workers, http://www.ufw.org/_page.php?menu=research&inc=history/03.html (last visited Jan. 24, 2016).

28. *See* Mark Bittman, *Time To Boycott Tuna Again?*, N.Y. Times, Sept. 20, 2011, http://opinionator.blogs.nytimes.com/2011/09/20/time-to-boycott-tuna-again.

29. *See* Lena H. Sun, *Antiabortion Protesters Target Clinic's Landlord Outside Child's Md. School*, Wash. Post, Sept. 12, 2011, http://www.washingtonpost.com/national/health-science/anti-abortion-protesters-target-clinics-landlord-outside-childs-md-school/2011/09/12/gIQAn8z2NK_story.html.

30. Peter D. Kinder, KLD Research & Analytics Inc., Socially Responsible Investing: An Evolving Concept in a Changing World 8–9 (2005).

31. *See, e.g*, Brayden G. King & Sarah A. Soule, *Social Movements as Extra-institutional Entrepreneurs: The Effect of Protests on Stock Price Returns*, 52 Admin. Sci. Q. 413, 415 (2007).

become an activist, the question then becomes: what action should that shareholder take? This Note seeks to answer that question.

2. Scale

Shareholder campaigns, whether promoting divestment or engagement, seek to effect change at different levels. The first-order goal of a shareholder campaign is to raise awareness among shareholders and gain their support. Although some activists point to the number of investors that a campaign has persuaded to support their shareholder-focused campaign as an indicator of success,[32] this is rarely the end point of a campaign. Broad support at the shareholder level could be seen as a sign of successful outreach and persuasion efforts, but support alone does not effect changes in behavior at the corporate level.

The next level of impact is the corporation itself. A corporation-focused campaign succeeds when the company has implemented the change that the activists sought. Beyond that, the activist may be seeking to have an industry-wide impact through the targeting of a single prominent company.[33] In that case, success will be determined by other companies in the industry adopting the sought-after practice.

For some shareholder campaigns, the ultimate goal is to cause a change in policy at the government level, and changing corporate behavior is only an intermediate step. For example, the anti-apartheid movement's ultimate goal was to change the policies of South Africa's government; forcing companies to withdraw was only a means to pressure the South African government.[34] In the present day, the BDS Movement is seeking to influence Israel's policy towards Palestine by pressuring companies doing business with the Israeli military or in the occupied territories.[35] Many campaigns seek to influence actors at multiple levels, seeking change at the investor, company, and government levels.[36]

The focus of this Note's analysis is on a tactic's ability to influence corporate behavior. Thus even if a campaign gains broad sup-

32. *See, e.g.*, BARGHOUTI, *supra* note 6, at 144; Press Release, 350.org, Over 100 Colleges and Universities Join 350.org Fossil Fuel Divestment Campaign (Nov. 29, 2012), http://math.350.org/press/.

33. Frank den Hond & Frank G. A. de Bakker, *Ideologically Motivated Activism: How Activist Groups Influence Corporate Social Change Activities*, 32 ACAD. MGMT. REV. 901, 916 (2007).

34. *See* Davis, *supra* note 7.

35. *See* BARGHOUTI, *supra* note 6.

36. SOULE, *supra* note 4, at 50.

port among shareholders and investors, it will not be considered a success for the purposes of this Note's analysis unless that broad support changes the target corporation's behavior. Conversely, if the campaign is successful at forcing a company to change policy, it would be considered a success even if the campaign's ultimate goal is to change the entire industry's practices or to influence government policy. This Note's metric of success is more limited than the metrics of success of broader social movements which can succeed (or fail) at multiple levels.

C. *Audiences for Shareholder Campaigns*

In efforts to alter company policy and behavior, the primary audience necessarily must be company leadership. A company's board of directors is charged with managing the business and affairs of the corporation.[37] The board hires (and fires) the company's chief executive officer, who in turn manages the operations of the company, hires the other senior officers, and works with the board to determine company strategy.[38] The directors and officers will be referred to collectively as a company's leadership. Except on extraordinary matters that require shareholder approval or where the company is subject to laws or regulation, company leadership has the sole discretion to determine company policy, direct the company's employees and agents, and allocate the company's resources.[39]

In order to press a shareholder campaign, activists will need to persuade shareholders to align with them and exercise their rights as shareholders accordingly. Sympathetic investors may elect to donate their stock to an activist organization outright, as happened in PETA's campaign against animal testing at Proctor & Gamble.[40] Activists may also purchase stock in order to engage with company leadership as shareholders themselves.[41] In this Note, references to "activist investors" will refer to shareholders acting to cause change for social or environmental reasons, so the concept includes shareholders who have allied with activists, shareholders who have de-

37. DEL. CODE ANN. tit. 8, § 141(a) (2014).

38. PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS §§ 3.01–3.02 (Am. Law Inst. 1994).

39. *Id.*; DEL. CODE ANN. tit. 8, §§ 141(a), 251(c) (2014); DEL. CODE ANN. tit. 8, §§ 271(a), 275(b) (2010).

40. SOULE, *supra* note 4, at 11.

41. *See, e.g.*, Stewart J. Schwab & Randall S. Thomas, *Realigning Corporate Governance: Shareholder Activism by Labor Unions*, 96 MICH. L. REV. 1018, 1081–82 (1998).

cided to take action for themselves, and activists who have purchased or received shares in order to conduct engagement efforts.

A corporation's shareholder body may be comprised of a variety of actors. The founders and leadership of a company may hold a substantial portion of the outstanding stock. Individual "household" or "retail" investors may own small stakes in a corporation as well. The ownership of corporate equity among retail investors has shrunk in comparison to the ownership in the hands of institutional investors[42]—organizations that pool large sums of money under unified management which invest in equities and other asset classes to provide returns for their investors. Pension funds, which manage retirement savings on behalf of workers in government or private companies, are one source of immense institutional wealth.[43] Mutual funds and index funds, which hold a diversified portfolio of stocks on behalf of investors, also represent a large percentage of equity ownership of the U.S. stock market.[44] Sovereign wealth funds, which manage the investable assets of a nation, and university endowments are another form of institutional wealth. Given the size of their holdings and centralized management, institutional investors are attractive targets for shareholder campaigns because they can be lobbied more efficiently than individual investors.

Shareholders may have different motivations for holding stock. Generally, they are motivated by investment returns in the form of increased share price and dividends. Some investors pursue a long-term investment in the company's growth, while others may take short-term, speculative positions. An example of the latter would be a hedge fund that buys a stake in a company in order to launch a profit-motivated shareholder campaign to boost the share price and then sells to capture the resulting gains. The types of investors and their motivations impact a shareholder campaign tactic's ability to persuade investors, which is a necessary precondition for a shareholder campaign and its ability to influence corporate leadership towards reform.

Shareholder campaigns and accompanying public relations efforts are meant to reach audiences outside the corporation as well

42. Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights,* 113 COLUM. L. REV. 863, 874–76 (2013).

43. *See* MANHEIM, *supra* note 17, 31.

44. *See* Gilson & Gordon, *supra* note 42, 886.

as within.[45] Shareholder campaigns are one means of reaching out to the general public to alert them to an issue, educate them on it, and persuade them to align with the activists' positions. Persuading members of the general public can lead to new supporters for the activist organization, create external opposition to the corporation, and provide political clout to influence lawmakers. Lawmakers and regulators are themselves an audience for shareholder campaigns, as they are subject to persuasion and are able to effect changes in the law that could prohibit or deter certain corporate malfeasance. Activists will also seek to entice the media to cover their efforts favorably, as a means of amplifying their messages directed at the groups discussed above.[46] Again, external audiences are only relevant to this analysis insofar as it may allow the activist to indirectly influence a company's leadership.

D. Exit and Voice Framework

In his seminal essay *Exit, Voice, and Loyalty*, economist Albert O. Hirschman set out a framework for decisions facing individuals involved with institutions, both governments and business organizations, which have suffered a lapse from virtuous behavior.[47] The actions available to such individuals can be roughly characterized as "exit" or "voice." The "exit" option is characterized as an economic mechanism, namely ceasing to purchase a firm's goods, usually in favor of a competitor's goods.[48] "Voice" is characterized as a political mechanism—engaging with the firm by expressing one's disapproval and seeking reform.[49] Hirschman goes on to examine the relative advantages of these two strategies.

In Hirschman's analysis, the choice between exit and voice is faced by customers when the quality of a firm's goods deteriorate.[50] However, the analysis has also been applied in the context of a firm

45. *See generally* Heidi J. Welsh, *Shareholder Activism*, 9 MULTINATIONAL MONITOR, no. 12, Dec. 1988, http://www.multinationalmonitor.org/hyper/issues/1988/12/mm1288_06.html.

46. Joakim Sandberg, *Changing the World through Shareholder Activism?*, 5(1) NORDIC J. APPLIED ETHICS, May 1, 2011, at 51, 68–69. *See, e.g.*, *Hold an Action*, 350.ORG, http://350.org/resources/hold-action/ (last visited Apr. 3, 2016) (advising activists that "[i]t's important to contact local, state, and national media to make sure they report on 350 actions in your area"); *Divestment*, BDS MOVEMENT, https://bdsmovement.net/activecamps/divestment (last visited Apr. 3, 2016) (naming "media exposure" as one of the tactics that divestment campaigners use).

47. ALBERT O. HIRSCHMAN, EXIT, VOICE, AND LOYALTY (1970).

48. *Id.* at 21–25.

49. *Id.* at 30.

50. *Id.* at 4.

departing from optimal profit-making behavior.[51] Shareholders can choose to "exit" the company by selling their shares.[52] This option, also known as taking the "Wall Street Walk,"[53] frees the investor to pursue more desirable investments. Alternately, shareholders may exercise "voice" by engaging with company leadership to seek a change in policy.[54] Ideally, the reforms would return the company to optimal profitability and increase the value of the investor's shares. The exit and voice framework has also been applied to anti-corporate protests generally[55] and shareholder responsibility specifically.[56]

This framework informs this Note's analysis of shareholders who seek change for environmental or social ends, rather than improving the value of their investment. The choice facing a shareholder activist mirrors that of any individual involved in an institution which suffers a lapse from virtuous behavior: exit—cutting off ties and isolating the institution—or voice—continuing engagement by pushing for virtuous change.[57]

The "exit" option is divestment, selling the shares or other financial interest in the corporation whose behavior is undesirable. The "voice" option is shareholder engagement, engaging with the corporation's decision-makers, other investors, and other constituencies using the means of communication available to shareholders. As with Hirschman's general framework and the application to profit-seeking shareholders, these two approaches offer different advantages and drawbacks to those seeking to induce socially beneficial changes.

II.
DIVESTMENT

Divestment is the deliberate withdrawal of capital from a company whose policies or practices the investor considers unethical.[58] Divestment most commonly consists of selling a company's stock.

51. *See* Anat R. Admati & Paul Pfleiderer, *The "Wall Street Walk" and Shareholder Activism: Exit as a Form of Voice*, 22 REV. FIN. STUD. 2645 (2009) (analyzing the impact of shareholders' "threat of exit" on managers).

52. *Id.* at 2646.

53. *Id.*

54. Elroy Dimson et al., *Responsible Investing: Does It Pay To Be Bad?*, CREDIT SUISSE GLOBAL INVESTMENT RETURNS YEARBOOK 17, 19 (2015).

55. *See* King & Soule, *supra* note 31, at 413.

56. *See* Dimson et al., *supra* note 54.

57. Hirschman, supra note 47.

58. *See, e.g.*, *What is Fossil Fuel Divestment?*, FOSSIL FREE, http://gofossilfree.org/what-is-fossil-fuel-divestment/ (last visited Sept. 21, 2016).

However, it may involve other sources of capital, such as selling a company's bonds or withdrawing money from a deposit account in a bank.[59]

A. *Goals*

The unique goals of divestment as a shareholder activist tactic break down into three rough, intertwined categories: disassociative, expressive, and consequentialist.[60] Disassociation is the embodiment of investors' desire to rid themselves of any relation to or complicity with a corporation's improper acts.[61] The closely related impulse of expression drives investors to divest as a means of expressing their ethical values.[62] Divestment in this context sends a message to the outside world about what the investor believes, a display of moral integrity and consistency.[63] It also may serve as an expression of condemnation of a corporation's behavior.[64] Divest-

59. *Id.*

60. Divestment campaigns serve a number of other general purposes such as educating the public about the issue and providing a rallying point for organizers. *See* Meg Voorhes, *The US Divestment Movement*, *in* HOW SANCTIONS WORK: LESSONS FROM SOUTH AFRICA 129, 134 (Neta C. Crawford & Audie Klotz eds., 1999). Shareholder engagement tactics serve these goals as well. Since these goals do not serve as a useful point of distinction between the two tactics, discussion of them is omitted.

61. Pietra Rivoli, *Making a Difference or Making a Statement? Finance Research and Socially Responsible Investment,* 13 BUS. ETHICS Q. 271, 273 (2003) (noting that some investors who engage in socially responsible investing ("SRI") "are motivated by a desire 'not to be associated with' or 'not to profit from' certain activities or industries"); Voorhes, *supra* note 60, at 134 ("Activists equated holding securities as encouraging companies to remain in South Africa and, therefore, as signaling support for apartheid."); *see also* Simon Chesterman, *The Turn to Ethics: Disinvestment from Multinational Corporations for Human Rights Violations – The Case of Norway's Sovereign Wealth Fund*, 23 AM. U. INT'L L. REV. 577, 588–89, 606–10 (2008) (discussing complicity in the context of the Norwegian Government Pension Fund's investment guidelines).

62. *See* Patrick Geddes, *Measuring the Risk Impact of Social Screening*, 1 (Aperio Group, Working Paper, 2011), http://www.aperiogroup.com/system/files/documents/measuring_the_risk_impact_of_social_screening.pdf.

63. *See* KINDER, *supra* note 30, 24 (discussing consistency in the context of SRI). *See, e.g.*, ROBERT KINLOCK MASSIE, LOOSING THE BONDS 325 (1997).

64. *See, e.g.*, Claremont Colleges Fossil Fuel Divestment Campaign, *An Open Response to Pomona's Rejection of Divestment*, THE STUDENT LIFE, Nov. 15, 2013, http://tsl.pomona.edu/articles/2013/11/15/opinions/4512-an-open-response-to-pomonas-rejection-of-divestment ("Divestment is most powerful in its ability to stigmatize the fossil fuel industry, which is necessary to erode its influence over American politics and the economy."); Chesterman, *supra* note 61, at 612–14 (discussing expressive effects of public announcement of divestment decisions of government pension fund).

ment as expression may provide an example to other investors or shame them into taking similar actions.

The Ford Foundation's actions in the early 1970s are a prime example of the impulse towards disassociation and expression driving investment decisions. In the wake of Campaign GM, a drive to force GM to act in a more socially responsible manner (especially with regards to Apartheid South Africa), the Ford Foundation undertook an examination of how its endowment was invested in order to ensure that its holdings reflected the mission of the Foundation.[65] As a result, the Foundation divested itself of some questionable holdings, developed criteria for analyzing future investments, and vowed to exercise its proxy voting rights in a more thoughtful manner.[66]

This paper seeks to analyze divestment's efficacy with regards to the third category: consequentialist goals. Consequentialism refers to the use of divestment to achieve concrete changes in corporate behavior, beyond just disassociation or expression.[67] In the words of the seminal work *The Ethical Investor*, this is the distinction between "moral purity" and "moral effectiveness."[68]

The basic theory of influencing corporate behavior directly through divestment is that the threat of selling a company's stock will provide an incentive for the company to reform or may deter it from transgressing in the first instance.[69] This paper will focus on the utility of divestment as a consequentialist tool used to punish, reward, deter, or incentivize corporate behavior. The measure of success in this regard will be the tactic's ability to change corporate behavior, not the number of investors who support the movement, which is sometimes cited as a metric of the impact that a divestment campaign has achieved.[70]

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65. Massie, *supra* note 63, 318–20.

66. *Id.* at 321.

67. Rivoli, *supra* note 61, at 273 ("[T]he prospect of 'making a difference' through investment activities undoubtedly has strong appeal to many socially conscious investors.").

68. John G. Simon et al., The Ethical Investor 25 (1972).

69. *See* Richardson, *supra* note 15, at 134 ("No longer were social investors satisfied merely to avoid profiting from immorality; instead, they also sought to improve the behaviour of others."); Chesterman, *supra* note 61, at 614 (investment decisions as threat and incentive).

70. *See, e.g.*, *Fossil Fuel Divestment FAQ's*, Swarthmore Mountain Justice, https://swarthmorealumnidivest.files.wordpress.com/2014/11/faq1-pager1.pdf (last visited Sept. 21, 2016).

B. Distinction from Socially Responsible Investing

To better illuminate the somewhat hazy distinction between the unique goals of divestment as a tactic for shareholder activism, a brief discussion of divestment's relationship with the concept of socially responsible investing ("SRI") is necessary. SRI is the practice of incorporating social or ethical goals into the management of a fund or an investor's portfolio, rather than strictly focusing on the traditional goals of increasing returns and minimizing risk.[71]

SRI employs "positive screening" and "negative screening."[72] The screening process is often facilitated by SRI codes of conduct that provide standardized criteria for compliance against which corporate behavior may be judged.[73] Positive screening is the practice of affirmatively pursuing investments that further non-monetary goals.[74] Positive screens seek out companies that engage in socially beneficial behavior or eschew socially irresponsible practices.[75] Another form of positive screen involves channeling capital to businesses located in a certain region with an aim towards economic development.[76] A fund may implement a screen with publicity or may do so quietly. For example, when a coalition of socially responsible funds began seeking out "companies that take a leadership role in eradicating sweatshops," it held a press conference to announce the move.[77] The clear implication of its statement was to shame companies that were using sweatshop labor.[78]

Negative screening is the practice of avoiding or selling off investments in companies with questionable policies.[79] Selling stock is an act of divestment—when a fund manager realizes that a com-

71. KINDER, *supra* note 63, at 3–4 (noting the varied definitions of the term 'SRI'); Rivoli, *supra* note 61, at 271.

72. Maria O'Brien Hylton, *"Socially Responsible" Investing: Doing Good Versus Doing Well In An Inefficient Market*, 42 AM. U. L. REV. 1, 9–10 (1992); Rivoli, *supra* note 61, at 271.

73. *Id.*; *see also* Richardson, *supra* note 15, at 137–38.

74. *Screening Your Portfolio*, SOCIAL FUNDS, http://www.socialfunds.com/page.cgi/article2.html (last visited Feb. 21, 2016).

75. *Id.*

76. *See* VERMONT STATE TREASURER'S OFFICE, SURVEY OF ECONOMICALLY TARGETED INVESTMENTS: OPPORTUNITIES FOR PUBLIC PENSION FUNDS (2014).

77. Kevin Galvin, *Investors Take a Stand Against Sweatshops*, ASSOCIATED PRESS, Sept. 19, 2006, http://www.apnewsarchive.com/1996/Investors-Take-a-Stand-Against-Sweatshops/id-fcd65a898552f7e5ed348694c5315671.

78. *Id.* (The coalition stated, "We deplore the pervasiveness of sweatshops in the apparel, footwear and toy industries both in the United States and abroadFalse We recommend action against companies, not countries or workers, for conducting business in violation of the law.").

79. Hylton, *supra* note 72.

pany is not compliant with the social criteria of the fund or a change in corporate policy renders them non-compliant, the manager will sell the stock in that company. For example, when a manager of a fund that avoids so-called "sin stocks" discovers that one of her portfolio companies is involved in alcohol sales, she will sell her holding in that company. Many of these acts are motivated by the investor's desire to avoid complicity in the company's behavior, rather than to shame the company into changing its behavior by publicizing the decision.[80] As an example, in the wake of the Sandy Hook Elementary School shooting, Cerberus Capital Management, a private equity firm, sold its ownership stake in Freedom Group, the gun company that made the AR-15 rifle used in the attack.[81] In its statement, Cerberus disclaimed any intention to change Freedom Group's policies, stating:

> [a]s a Firm, we are investors, not statesmen or policy makers. . . . We believe that this decision allows us to meet our obligations to the investors whose interests we are entrusted to protect without being drawn into the national debate that is more properly pursued by those with the formal charter and public responsibility to do so.[82]

In these cases, the socially responsible investment decisions are more informed by disassociative ends and not properly viewed as consequentialist attempts to affirmatively influence the corporation's behavior.[83]

On the other hand, where negative screening involves avoiding the purchase of a company's stock in the first instance due to ethical concerns, there is no sale of the stock, and so this would not, strictly speaking, constitute an act of divestment. However, this passive screening may be done conspicuously in order to punish bad corporate behavior and to incentivize reform. For example, Calvert Investments provides SRI index funds which are composed of companies that are included in an index of socially responsible companies which they maintain; Calvert periodically reviews companies for ESG compliance to determine whether they should be added to

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80. *See* Chesterman, *supra* note 61, at 588–89 n.38.

81. Peter Lattman, *In Unusual Move, Cerberus To Sell Gun Company,* N.Y. TIMES DEALBOOK (Dec. 18, 2012, 5:54 AM), http://dealbook.nytimes.com/2012/12/18/cerberus-to-sell-gunmaker-freedom-group.

82. Press Release, Cerberus Capital Management, Cerberus Capital Management Statement Regarding Freedom Group, Inc., (Dec. 18, 2012), http://www.cerberuscapital.com/cerberus-capital-management-statement-regarding-freedom-group-inc.

83. *See* SIMON ET AL., *supra* note 68, at 52–53.

or removed from the index.[84] When Calvert decides to drop a company from an index it issues a press release noting why the company has been dropped.[85] In this context, a decision to refrain from purchasing a stock would resemble a passive form of divestment undertaken for consequentialist ends.

The analysis here focuses on the use of divestment as a consequentialist tool used to punish, reward, deter, or incentivize corporate behavior, as distinct from non-public acts of divestment taken for disassociative reasons. Thus, the distinction between the motivations underlying the investment decision is more salient than the distinction between passive and active investment actions, so passive negative screening employed to alter corporate behavior can be understood as a type of divestment action for the purposes of this analysis. In most cases, it is reasonable to assume that investors choose SRI for a mix of disassociative, expressive, and consequentialist goals.[86]

C. *Distinction from Disinvestment*

It is important to make another distinction: the differences between what I will call "disinvestment" and divestment. In the business world, "divestment" is used to refer to the sale of particular assets or removal of capital from a specific enterprise.[87] The term may be used synonymously with divestiture or disinvestment—selling important assets or spinning off a particular division of a company.[88] In this context, divestment is undertaken to abandon an

84. *The Calvert Responsible Index Series*, CALVERT INVESTMENTS, http://www.calvert.com/NRC/literature/documents/br10092.pdf.

85. *See, e.g.*, Press Release, Calvert, Calvert Social Index Announces the Deletion of Whiting Petroleum from the Calvert Social Index (Mar. 20, 2015), http://www.calvert.com/media-relations/press-releases/whiting-petroleumn-deletion-from-calvert-social-index (dropping Whiting Petroleum for failure to meet sustainability criteria); Press Release, Calvert, Calvert Social Index Actions, (May 22, 2009) http://www.businesswire.com/news/home/20090522005062/en/Calvert-Social-Index-Actions (dropping Weyerhaeuser Company for failure to meet indigenous peoples' rights criteria).

86. Insofar as a divestment campaign requires a large number of investors to divest in order to drive a company's stock price down, those who refrain from investment in a company based on SRI screens may be counted among the converts. Since the economic consequences of negative screening have been more thoroughly researched than divestment campaigns, this Note will rely on insights from that research where appropriate.

87. *Divestment*, INVESTOPEDIA, http://www.investopedia.com/terms/d/divestment.asp (last visited Feb. 20, 2016).

88. *Id.* ("Generally you'd just say that you are selling an asset. The term divestment is more appropriate however in the following contexts: 1) A change in corpo-

unprofitable line of business or to exit a particular country or region. Disinvestment is sometimes used to refer to socially-oriented investment decisions,[89] but divestment is used far more frequently in the relevant literature. Therefore, I will refer to businesses selling assets as "disinvestment" and maintain a narrow definition of divestment as the selling of investments for environmental or social ends by an investor.

Distinguishing between the two concepts in this way is a semantic choice, but the distinction is important. Divestment is sometimes used interchangeably for both meanings in the literature discussing social movements, especially with regards to the anti-Apartheid movement.[90] Divestment has been used to refer to the general strategy of pressuring companies to stop doing business in South Africa; that campaign employed a range of tactics.[91] Such a strategy would be more accurately termed "compelling disinvestment." Divestment has also been used to refer to the particular tactic of systematically persuading individual and institutional investors to sell their stock in companies doing business in South Africa.[92] That effort would be properly called "a divestment tactic."

The conflation of these two concepts has created a misunderstanding regarding the degree of success that the anti-apartheid divestment campaign achieved. While the strategy to compel disinvestment was no doubt successful, as evidenced by the flight of U.S. corporate capital from South Africa in the late 1980s,[93] the degree to which the tactic of divestment contributed to this success is far from clear.[94] Divestment was only one of the pressure tactics employed, along with protests, press releases, and selective purchasing laws, whereby U.S. cities and local governments would boycott

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rate strategy - a firm might say that they are divesting a particular subsidiary to focus on their core business. 2) Social goals - there are many political reasons why investors might reduce investments. A notable example was the withdrawal of American firms from South Africa during apartheid.").

89. *See* Chesterman, *supra* note 61, at 588 n.37 ("Disinvestment is used here to indicate the selling of assets for ethical purposes.").

90. Brennan, *supra* note 1.

91. *See, e.g.*, Neta C. Crawford, *Trump Card or Theater? An Introduction to Two Sanctions Debates*, *in* HOW SANCTIONS WORK: LESSONS FROM SOUTH AFRICA 3, 15 (Neta C. Crawford & Audie Klotz eds., 1999).

92. *See* Simon Rottenberg, *The Universities and South Africa: The Campaign for Divestment*, 24 MINERVA 223 (1986).

93. LANDIER & NAIR, *supra* note 11, at 20.

94. SOULE, *supra* note 4, at 87 ("Although there was some evidence that corporate disinvestment might pressure the South African government to end apartheid, it was clear that corporate decisions to disinvest were rarely, if ever, based on universities divesting of their stock."(internal citations omitted)).

companies with operations in South Africa.[95] While some investors chose to divest, other sympathetic investors chose to pursue shareholder engagement tactics.[96] So it is difficult to disaggregate the impact of divestment from the broader campaign.

Corporate executives certainly noted divestment efforts, but felt that it had "no direct economic impact" on their companies.[97] Subsequent empirical research supports this observation.[98] Executives were more concerned with the impact of the selective purchase acts,[99] which had the capacity to directly impact the companies' revenues. Thus, when the proponents of modern-day divestment campaigns cite the campaign to compel disinvestment from South Africa as an example of a successful divestment campaign,[100] they are standing on shaky ground.

III.
ENGAGEMENT

Shareholder engagement is action undertaken by a company's shareholders with the goal of changing the conduct of a firm in order to better respond to the shareholder's financial, social, or ethical expectations.[101] While a shareholder may take action in her capacity as a private individual or institution, as an employee, or as a citizen,[102] this paper will focus on acts done in the shareholder's

95. Voorhes, *supra* note 60, at 135, 138; Welsh, *supra* note 45 ("Shareholder activists, however, can claim only partial responsibility for gains in this area; many complex factors came into play. Restrictive contracting requirements by major U.S. cities and states have been at least as important as shareholder resolutions and adverse publicity.").

96. *See id.* at 136.

97. *Id.* at 130.

98. *See infra* Part IV.B.1; *see also* Siew Hong Teoh, Ivo Welch & C. Paul Wazzan, *The Effect of Socially Activist Investment Policies on the Financial Markets: Evidence from the South Africa Boycott*, 72 J. BUS. 35 (1999).

99. Voorhes, *supra* note 60, at 130, 139.

100. *See, e.g.*, Bill McKibben, *Global Warming's Terrifying New Math*, ROLLING STONE, July 19, 2012, http://www.rollingstone.com/politics/news/global-warmings-terrifying-new-math-20120719?page=3); BARGHOUTI, *supra* note 6, at 149–50 (citing the anti-apartheid divestment movement as a template for success for their own citizen-led movement); s*ee also* Welsh, *supra* note 45 ("The corporate exodus from South Africa since 1985 is the most frequently cited example of shareholder victory.").

101. Bruno Amann et al., *Shareholder Activism for Corporate Social Responsibility*, *in* THE NEW CORPORATE ACCOUNTABILITY, 337 (Doreen McBarnet et al. eds. 2009).

102. For example, an executive who owns stock may make a management decision which affects the corporation's policies, or a retail investor may volunteer with a political campaign which affects issues of concern to the corporation.

capacity as an investor, utilizing the means of activism that are uniquely available to shareholders.

A. Goals

The unique goals of shareholder engagement are expressive and consequentialist. Unlike divestment, engagement does not further any disassociative ends, as the shareholder must maintain her stockholding and communicate actively with the company's leadership and other constituencies. The expressive goals are simple to understand: the activist communicates to corporate leadership, stakeholders, and the public that she wants the company to change. Pursuing a "voice" strategy also implicitly communicates that the activist believes that the company is capable of reform and may respond to her efforts.[103] The general consequentialist aims of engagement are identical to those of divestment: to influence behavior of corporations towards ethical and sustainability goals.[104]

B. Methods

1. Shareholder Voting Power

The right to cast a vote on important matters affecting the company is one of the fundamental rights of a shareholder.[105] The most critical subject of shareholder votes is the election of directors to the board (or their removal from the board).[106] The power to control the corporation's conduct and policies resides in the hands of the board, not the shareholders.[107] However, the shareholders have the ability to influence the board through the vote, namely by expressing disapproval of the decisions of the board or a particular director by voting against her appointment or by withholding the shareholders' votes.[108] Shareholder votes are also required to approve amendments to the articles of incorporation, major transactions such as a sale of the company, and shareholder resolutions regarding changes in company policy.[109]

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103. *See* Hirshchman, *supra* note 47, at 38.

104. Chesterman, *supra* note 61, at 587–88.

105. Julian Velasco, *The Fundamental Rights of the Shareholder*, 40 U.C. DAVIS L. REV. 407 (2006).

106. Paul H. Edelman et al., *Shareholder Voting in an Age of Intermediary Capitalism*, 87 S. CAL. L. REV. 1359, 1368 (2014).

107. Sandberg, *supra* note 46, at 54.

108. Edelman et al., *supra* note 106, at 1365–69.

109. *See* Adam J. Sulkowski & Kent Greenfield, *A Bridle, a Prod, and a Big Stick: An Evaluation of Class Actions, Shareholder Proposals, and the Ultra Vires Doctrine as Methods for Controlling Corporate Behavior*, 79 ST. JOHN'S L. REV. 929, 937 (2005).

Votes take place at the company's annual shareholder meeting or at special meetings called by the board.[110] Ballots are usually cast via proxies sent in by shareholders rather than in person at the meeting.[111] Generally the number of votes a shareholder is entitled to cast is proportional to the number of shares she owns, allowing large shareholders to have a greater influence on the outcome of votes.[112]

As with elections for public office, shareholder votes may be accompanied by shareholders campaigning for a specific agenda. For example, activist shareholders may seek to garner shareholder support for a "vote no" campaign to oppose the candidacy of a director in order to express dissatisfaction with the direction of the company.[113] Boards have become increasingly responsive to these shareholder campaigns.[114]

2. Shareholder Resolutions

Shareholder resolutions are the primary tool in the activist investor's toolkit. Public corporations are required to allow shareholders to place resolutions on the management's proxy statement for consideration and voting by Rule 14a-8 of the Securities and Exchange Act.[115] The shareholder resolution as a tool to achieve social goals has increased in frequency and prominence.[116] Not only are more resolutions being filed, but shareholder support for these initiatives is increasing.[117] In 2002, proposals advancing social goals averaged less than ten percent support among shareholders; by 2011, that figure had increased to more than twenty percent.[118] In 2004, fewer than thirty resolutions focused on sustainability received more than twenty percent support, according to Fund

110. Sandberg, *supra* note 107, at 55.

111. William L Megginson & Scott B. Smart, Introduction to Corporate Finance 198 (2009).

112. *Id.* Note that some classes of stock may enjoy "super-voting" status. This stock is usually retained by company insiders so they may retain control of the company. *See* Investopedia Staff, *Why Would a Company Have Multiple Share Classes, and What Are Super Voting Shares?*, Investopedia, http://www.investopedia.com/ask/answers/05/070405.asp (last visited Apr. 10, 2016).

113. Landier & Nair, *supra* note 11, at 33.

114. *Id.*

115. 17 C.F.R. § 240.14a–8 (2016).

116. *See, e.g.*, James Copland, *Special Report: Shareholder Activism by Socially Responsible Investors*, Proxy Monitor (2014), http://www.proxymonitor.org/Forms/2014Finding4.aspx.

117. Sach, *supra* note 14, at 934.

118. *Id.*

Votes.[119] By 2013 approximately 100 sustainability resolutions hit that threshold.[120]

The impact of these resolutions is not entirely clear. Corporate law in Delaware, the state of incorporation for the majority of large U.S. companies,[121] places the ultimate authority for making decisions regarding a company's management in the board of directors.[122] Coupled with the fact that Rule 14a-8 allows a proposal to be excluded if it is improper under state law,[123] this mandate requires that shareholder proposals not bind the board to take specific actions. So "virtually all proposals must be in precatory form."[124] Further, even if a proposal obtains a majority, the board is not legally obligated to enact the changes if they conclude that doing so is not in the best interests of the corporation.[125]

While enacting the change is not legally required, failure to enact a majority vote resolution can generate negative publicity and harm shareholder relations, which creates pressure on the board to enact the change.[126] For example, in 2002 the board of Cracker Barrel voted unanimously to change the company's employment policies to prohibit discrimination based on sexual orientation after a proposal submitted by a New York City pension plan garnered fifty-eight percent of the proxy vote.[127] The company had withstood pressure from shareholders and external tactics, including a consumer boycott and class action discrimination lawsuit, for over ten years prior to its reversal.[128]

In other instances, even a resolution that fails to achieve majority support may still succeed at convincing management that the

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119. *Companies Face Record Number of Shareholder Resolutions Urging Action on Environmental Issues*, IW FINANCIAL (Mar. 24, 2014), http://news.iwfinancial.com/corporate-sustainability/companies-face-record-number-of-shareholder-resolutions-urging-action-on-environmental-issues/.

120. *Id.*

121. Lucian Ayre Bebchuk & Alma Cohen, Firms' Decisions Where to Incorporate, 46 J. L. & ECON. 383, 389 (2003).

122. DEL. CODE ANN. tit. 8, § 141(a).

123. 17 C.F.R. § 240.14a-8(i)(1) (2016).

124. Sach, *supra* note 14, at 936.

125. *See* Andrew R. Brownstein & Igor Kirman, *Can a Board Say No when Shareholders Say Yes? Responding to Majority Vote Resolutions*, 60 BUS. LAW. 23, 39 (2004).

126. *See id.* at 24.

127. Sulkowski & Greenfield, *supra* note 109, 939–43.

128. *Id.* at 939–40. The Cracker Barrel reversal was particularly significant because the company's efforts to exclude a previous proposal had resulted in a controversial SEC No-Action letter in 1991 which categorically prohibited resolutions relating to employment based on the ordinary business exclusion discussed above. The SEC reversed its position in 1998.

measure is worth implementing.[129] This happens rarely but can be seen in some cases where the resolution garners a significant portion of the voted shares.[130] If the measure is successful at gaining traction with the public or appears likely to do so, it will create additional pressure on management to concede to the activists' demands before the resolution comes up for a vote.[131]

Support for a proposal may also provide impetus for the company's leadership to engage with the activists to address their concerns through direct negotiations.[132] Company leadership may also preemptively engage with shareholder advocates before the proxy is sent out. If negotiations result in concessions that the activists find satisfactory, they will withdraw their proposal before it comes up for a vote.[133]

Shareholder resolutions crafted for social or environmental impact take several forms. A common form is a resolution calling for an impact study or sustainability report, wherein a company investigates the impact that its operations will have on a certain phenomenon or what impact the phenomenon will have on the company's operations, and then discloses the results.[134] For example, the Interfaith Center on Corporate Responsibility proposed a resolution that called on Exxon to form a committee of outside directors to review the impact of climate change on Exxon's policies and practices and to work toward reducing emissions.[135]

A related proposal archetype calls for the company to disclose information regarding certain aspects of their business, usually with an aim toward concentrating management's attention on a certain matter or highlighting a particular problem. For example, a 2013

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129. *See* Emily Chasan, *More Companies Bow to Investors with a Social Cause*, WALL ST. J. (Apr. 1, 2014, 2:44 AM), http://blogs.wsj.com/cfo/2014/04/01/more-companies-bow-to-investors-with-a-social-cause (discussing a resolution urging Home Depot to stop selling wood from old-growth forests that only garnered 12% of the vote but which the company still chose to implement).

130. Sach, *supra* note 14, at 932.

131. *See* LANDIER & NAIR, *supra* note 11, at 35; Sach, *supra* note 14, at 932.

132. Rivoli, *supra* note 61, at 275.

133. *See* Sach, *supra* note 14, at 932, 940.

134. *See, e.g.*, *Companies Face Record Number of Shareholder Resolutions Urging Action on Environmental Issues*, *supra* note 119 (discussing sustainability reports); *Study Finds Racial and Economic Bias in Western Union Practices*, CONSUMERACTION (June 2008), http://www.consumer-action.org/radar/articles/study_finds_racial_and_economic_bias_in_western_union_practices/ (last visited Apr. 10, 2016) (describing a resolution calling on Western Union to issue a report on community reinvestment).

135. Martha M. Hamilton, *Shareholders Defy Exxon over Global Warming Measure*, WASH. POST, April 30, 1998, at D2.

shareholder resolution urged Exxon to disclose "quantitative data on its efforts to safeguard the public and the environment" from its fracking operations.[136] Such measures may also reveal and emphasize particular areas of risk that may translate into future financial losses, which are potentially of interest to purely financial investors. A similar type of resolution calls for companies to come into compliance with certain standards, like international efficiency or workplace standards. For example, activist investors in the anti-Apartheid movement pushed companies to adopt the Sullivan Principles, a code of conduct for the treatment of black workers in South Africa.[137]

Resolutions that call for specific changes to policies or practices are rare, likely because of the constraints of Delaware law mentioned above. These generally are used where the desired policy has already become widely adopted within the industry and the target company can be characterized as an outlier.[138] For example, in 2013 the New York City pension funds were able to convince four major U.S. corporations to expand their equal employment policies to include gender discrimination.[139]

3. Shareholder Meetings[140]

Shareholders also have the right to attend the company's annual meeting and any special meetings called by the board.[141] The

136. OFFICE OF THE NEW YORK CITY COMPTROLLER, 2013 SHAREOWNER INITIATIVES: POSTSEASON REPORT 4 (Fall 2013), http://comptroller.nyc.gov/wp-content/uploads/documents/NYC_Shareowner_Initiatives_-_2013_Postseason_Report.pdf. While the resolution received an impressive 30.2% of the votes cast, ExxonMobil leadership did not agree to produce the report.

137. Voorhes, *supra* note 60, at 132.

138. *See, e.g.*, Sarah Kershaw, *Wal-Mart Sets a New Policy that Protects Gay Workers*, N.Y. TIMES (July 2, 2003), http://www.nytimes.com/2003/07/02/us/wal-mart-sets-a-new-policy-that-protects-gay-workers.html?pagewanted=all (noting the successful use of shareholder resolutions to pressure General Electric and McDonald's to adopt non-discrimination policies based on sexual orientation, which the majority of Fortune 500 companies had already adopted).

139. OFFICE OF THE NEW YORK CITY COMPTROLLER, *supra* note 136, at 15.

140. In addition to the right to attend meetings, Delaware law grants shareholders the right to inspect a corporation's books and records "for any proper purpose." *See* David Millon, *Shareholder Social Responsibility*, 36 SEATTLE U. L. REV. 911, 924–28 (2013) (discussing "strategic CSR"). They may also sue executives and directors on behalf of the corporation in a shareholder derivative suit. While these rights may provide an attractive mechanism for revealing information about a corporation's social and environmental performance or for exerting pressure on management, these rights are rarely exercised by activists.

141. DEL. CODE ANN. tit. 8, § 211 (West).

company may exclude any non-shareholders from attending.[142] These meetings provide shareholders with a venue to ask questions of the board of directors and key officers. Usually, this is a chance for shareholders to ask questions of company management about strategy or other matters affecting the company's business. However, for shareholders with a social agenda, it provides the opportunity to ask pointed questions of management about their issues.[143] As with a politician facing a hostile press corps, directors facing tough questions regarding questionable practices may suffer embarrassment in front of the shareholders, directors, and, if reporters are covering the meeting, the press.[144] In addition to embarrassing the company's leadership, the meeting provides the activists with a chance to educate the other shareholders in attendance. Shareholder activists may, in essence, turn the shareholder meeting into a site of political contestation.[145]

The activist may choose to take a more confrontational stance and attempt to disrupt the meeting. This can involve unfurling banners or shouting from the crowd during management's presentation. For example, in 1967 a community organizing group pushing for more inclusive employment practices at Kodak bought Kodak shares and had representatives cause disruptions in the annual meeting, while 600 protestors demonstrated outside.[146] Shortly thereafter, the group and Kodak reached an agreement providing for inclusive training and business development opportunities.[147]

As disruptive tactics have become commonplace, companies are advised to take precautionary measures for the annual meeting, such as limiting attendance to shareholders, enforcing speaking time limits, and establishing strict security protocols to minimize

142. Craig M. Garner & Chris G. Geissinger, Annual Meeting Handbook 56 (RR Donnelly 2015).

143. *See, e.g.*, *Admission Credentials Needed for Coca-Cola's Annual Meetings*, The Campaign to Stop Killer Coke, http://killercoke.org/events.php (last visited January 30, 2016) ("The annual meeting is the only place where we can challenge Coke's chief policymakers—the top executives and members of the company's board of directors—face-to-face.").

144. *See, e.g.*, Alice Schroeder, The Snowball: Warren Buffett and the Business of Life 635–37 (2008) (describing a particularly contentious Coca-Cola shareholder meeting as "the most disastrous shareholder meeting in Coca-Cola history" and a "fiasco").

145. Soule, *supra* note 4, at 10 (citing Vogel, David, Lobbying the Corporation: Citizen Challenges to Business Authority (1978)).

146. Quilen Diedre Blackwell, *Holding Corporate America's Feet to the Fire*, 15 Comm-Org Papers (2009), https://comm-org.wisc.edu/papers2009/blackwell.htm.

147. Soule, *supra* note 4, at 60.

any disruptions.[148] Even for tough questions posed during the Q&A period, management will usually have prepared stock responses that will minimize the impact of any critical feedback.[149]

4. General Engagement

Shareholders also have the power to communicate directly with company leaders using informal means such as e-mail, letters, and phone calls.[150] Activists may conduct these communications in private or may publicize them, such as using "open letters."[151] There is a strong norm that company boards should communicate with their shareholders.[152] For example, the New York Stock Exchange even requires companies to disclose a means for shareholders to directly contact independent directors in their proxy statements.[153]

Activist shareholders often engage with company leadership informally before resorting to the shareholder resolution.[154] Alternately, an activist shareholder may simply submit a resolution as the first step in a negotiation process and then withdraw it if negotiations prove successful.[155] About thirty percent of environmental and social shareholder resolutions are withdrawn upon the shareholder engaging in productive negotiations with company leadership.[156] Where the activist is a large, well-respected institutional investor, the company may be eager to engage with the activist rather than face a shareholder resolution. For example, a study of

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148. GARNER & GEISSINGER, *supra* note 142, at 55–57. *See also, e.g.*, ROBERT J. FOSTER, COCA-GLOBALIZATION: FOLLOWING SOFT DRINKS FROM NEW YORK TO NEW GUINEA 209 (2008) (noting Coca-Cola's efforts to restrain disruptions at annual meetings, including imposing strict time limits on speakers and forcibly removing unruly speakers).

149. *See* GARNER & GEISSINGER, *supra* note 142, at 56–57.

150. MARC GOLDSTEIN, INSTITUTIONAL SHAREHOLDER SERVICES, DEFINING ENGAGEMENT: AN UPDATE ON THE EVOLVING RELATIONSHIP BETWEEN SHAREHOLDERS, DIRECTORS, AND EXECUTIVES, INSTITUTIONAL SHAREHOLDER SERVICES 14–15 (Apr. 10, 2014), http://irrcinstitute.org/wp-contest/uploads/2015/09/engagement-between-corporations-and-investors-at-all-time-high1.pdf.

151. Willard D. Carleton et al., *The Influence of Institutions on Corporate Governance through Private Negotiations*, 53 J. FIN. 1335, 1339 (1998).

152. THE CONFERENCE BOARD GOVERNANCE CENTER, RECOMMENDATIONS OF THE TASK FORCE ON CORPORATE/INVESTOR ENGAGEMENT 9 (2013) ("Directors should take into account investors' viewpoints on the governance and strategy of the corporation in the exercise of their fiduciary duties to all investors and to the company as a whole.").

153. N.Y. Stock Exchange Listed Company Manual § 303A.03.

154. Rivoli, *supra* note 61, at 275.

155. Carleton et al., *supra* note 151, at 1338–39.

156. Chasan, *supra* note 129.

the engagement efforts of TIAA-CREF, the single largest pension fund in the United States, found that when the fund engaged with eighteen companies over the issue of board diversity, seventeen had increased their board diversity within five years of the engagement.[157]

C. Distinction from Shareholder Activism

It is worth drawing a distinction between shareholder engagement and "shareholder activism." Some shareholders, typically hedge funds, will engage with a company's leadership on issues of corporate governance, executive compensation, or business strategy.[158] These efforts are usually motivated by the desire to increase the value of the investor's shareholding, to prevent a decrease in value, or simply to improve management's responsiveness to shareholders.[159]

The term "shareholder activism" encompasses both efforts motivated by profit and efforts motivated by environmental or social goals.[160] But the term is used more often in the context of corporate governance or business strategy changes rather than in the context of environmental or social changes, so this Note uses the term "engagement" instead. However, the term "activist investor" is used in both contexts and will be used here in the sense of activism meant to achieve environmental or social goals.

In practice, this distinction is not always clear. Many socially responsible acts can have ancillary benefits to a company's bottom line. For example, Wal-Mart's efforts to use energy efficient lighting in new stores will reduce energy consumption, which will be beneficial to the environment while also reducing operating costs.[161] On the other hand, many acts undertaken for profitability improve-

157. Carleton et al., *supra* note 151, at 1337.

158. PRICE WATERHOUSE COOPER, SHAREHOLDER ACTIVISM: WHO, WHAT, WHEN, AND HOW? 2–3 (2015), https://www.pwc.com/us/en/corporate-governance/publications/assets/pwc-shareholder-activism-full-report.pdf.

159. Glenn Curtis, *Could Your Company Be a Target for Activist Investors?*, INVESTOPEDIA, http://www.investopedia.com/articles/stocks/08/activist-investor.asp (last visited Apr. 10, 2016).

160. *See, e.g.*, Dunstan Prial, *Shareholder Activism More Focused, Targeted*, FOX BUSINESS (May 25, 2012), http://www.foxbusiness.com/features/2012/05/25/shareholder-activism-more-focused-targeted.html (quoting Jim Copland, "[T]he growth in activism has been spearheaded over the past decade primarily by groups falling into two categories: those whose motives are purely profit driven and those whose motives are more ideological.").

161. Jeffrey Goldberg, Annals of Spin: Selling Wal-Mart, THE NEW YORKER, Apr. 2, 2007.

ment have ancillary social benefits. For example, PepsiCo's decision to source corn locally in Mexico reduced transportation costs and increased quality while also improving local education, increasing savings rates, and discouraging marijuana cultivation.[162] Taking a capacious view of the long-term value of being a good corporate citizen, sometimes referred to as "enlightened shareholder value,"[163] any socially or environmentally responsible action can be seen as a value-increasing maneuver.[164] Conversely, if one adopts Milton Friedman's view that a corporation's sole responsibility to society is to increase profits,[165] any action taken with a view towards improving the bottom line can be seen as a socially beneficial move. Similarly, many commentators have stressed the positive role that active institutional investors can play in the economy while lobbying management in their own self-interest.[166] Better corporate governance can improve the functioning of the economy and capital markets by reducing waste, deterring and preventing fraud, and improving the quality of disclosures.[167]

Depending on how broadly one views long-term value and the social value of profit-seeking behavior, there can be significant overlap between profit-seeking motivations and social motivations. For the purposes of this Note's analysis, it is not necessary to stake out a position along this spectrum. It is sufficient to say that this Note's focus is on shareholder action motivated by environmental or social ends, rather than value maximization. The value of the investment is only relevant to this inquiry insofar as it impacts the relative costs of conducting shareholder engagement. This Note does not focus on campaigns for corporate governance reforms. Corporate governance reforms can increase management's responsiveness to shareholders. However, since we cannot be sure that a given shareholder body will be motivated by social beneficence, it is not a foregone conclusion that such reforms will lead to positive outcomes for society. Therefore, without taking a position on the social utility

162. Stephanie Strom, *For Pepsi, a Business Decision with Social Benefit*, N.Y. TIMES, Feb. 22, 2011, at B1.

163. *See, e.g.*, Virginia Harper Ho, *"Enlightened Shareholder Value": Corporate Governance Beyond the Shareholder-Stakeholder Divide*, 36 IOWA J. CORP. L. 59, 61 (2010).

164. *See* Millon, *supra* note 140, 926.

165. Milton Friedman, *The Social Responsibility of Business Is To Increase Its Profits*, N.Y. TIMES MAG., Sept. 13, 1970, at 32.

166. IRIS H-Y CHIU, FOUNDATIONS AND ANATOMY OF SHAREHOLDER ACTIVISM 33–36 (2010).

167. *Id.*

of corporate governance reforms, this Note excludes such campaigns from its analysis.[168]

IV. ANALYSIS

A. *Costs of Pursuing the Tactic*

In analyzing the utility of the two tactics, it is necessary to understand the costs of employing each approach. Activists for environmental and social causes have limited resources to pursue their goals.[169] Assuming the tactics offer equal probabilities of success, where one tactic costs less to implement, it will provide a greater return on activists' scarce resources. Lower costs will also increase the likelihood of achieving support among investors seeking financial gains from their investment, increasing the chances that the tactic will succeed in changing corporate behavior.

Both tactics involve general organizing efforts: identifying attractive corporate targets, identifying shareholders, conducting outreach and education of shareholders, and publicizing the effort. These activities involve significant investments in time, effort, and expense. However, both divestment and shareholder engagement would require these general expenses—organizing and publicity costs do not significantly distinguish the two methods. Thus, separate discussion of general organizing costs is omitted and the following analysis will focus on costs that are unique to each tactic.

1. Divestment

Divestment imposes certain costs at the outset, but surprisingly does not necessarily impose long-term costs on investors. Selling a stock generally imposes transaction costs, such as commissions and fees.[170] Studies vary on the amount of transaction costs of divesting, from as little as 1% to 6% of the amount divested.[171]

Timing issues may also impose costs on the divestor. Unconstrained stockholders are free to time the sale of their stock to maximize their return by waiting for an opportune time to "sell high."

168. Research focused on or including activism for corporate governance reform will be considered where it is analogous to activism for social and environmental reform.

169. Millon, *supra* note 140, at 38.

170. *Transaction Costs,* INVESTOPEDIA, http://www.investopedia.com/terms/t/transactioncosts.asp (last visited Apr. 10, 2016).

171. PENSION CONSULTING ALLIANCE, ACADEMIC AND MARKET RESEARCH ON DIVESTMENT 6 (2014).

The investor who adopts the moral logic of divestment loses that advantage. However, even experienced investors will say that market timing is a fool's errand,[172] so the actual financial loss may be illusory.

Timing a sale also has tax implications. Selling stock is a realization event for tax purposes,[173] forcing the selling investor to recognize capital gains from the sale rather than continued deferral of taxation on the increase of the stock's value. Of course, where the stock has decreased in value, recognizing the loss will constitute a tax benefit. Thus, when divestors lose the ability to time their sale, the real loss is not strictly financial—selling at the right time could as easily result in superior investment returns or tax benefits—but rather the loss of flexibility in timing when those gains or losses are taken.

In addition to costs related to the sale of stock, applying a constraint to an investment portfolio can result in two types of costs: lower returns and increased risk.[174] Selling a stock requires the investor to substitute an alternative investment. Intuitively, one might expect this change to decrease returns, as the investor presumably viewed the stock position as a lucrative investment prior to divestment. However, several studies have contradicted this intuition. A meta-analysis found a positive association between corporate social performance and financial performance.[175] A study by S&P Capital IQ showed that an endowment that had divested from the fossil fuel industry, as the Fossil Free campaign calls for, would have achieved gains over the past ten years that were superior to a neutral portfolio.[176] When a task force considering divesting Connecticut state

172. *See, e.g.*, NICK MURRAY, SIMPLE WEALTH, INEVITABLE WEALTH 83–85 (5th ed. 2013).

173. 26 C.F.R. § 1.1001-1(a) (2016).

174. *See, e.g.*, Jacquelyn Humphrey & David Tan, *Does It Really Hurt To Be Responsible?*, 122 J. BUS. ETHICS 375, 376 (2014).

175. Marc Orlitzky, Frank L. Schmidt, & Sara L. Rynes, *Corporate Social and Financial Performance: A Meta-analysis*, 24 ORG. STUD. 403, 423 (2003). It should be noted that a causal relationship between corporate social performance and financial performance was not found.

176. Kevin Begos & Joann Loviglio, *College Fossil Fuel Divestment Movement Builds*, YAHOO! NEWS (May 22, 2013), http://www.yahoo.com/news/college-fossil-fuel-divestment-movement-builds-173849305.html?ref=gs. These results have been borne out by results from portfolios which have actually divested. *See* Kristen Domonell, *Is Fossil Fuel Divestment a Wise Move?*, UNIV. BUS. (June 2013), http://www.universitybusiness.com/article/divestment-debate ("In terms of generating competitive investment returns, Unity [College]'s endowment portfolio has met or exceeded market benchmarks over the past five years despite the shift away from fossil fuel holdings, says Deborah Cronin, vice president of finance and administra-

funds from companies doing business in Apartheid South Africa commissioned reports on the financial impact of divestment, all three investment firms who performed statistical analysis on potential returns found that a South Africa-free portfolio would provide superior returns.[177] Several studies have shown that SRI portfolios achieve returns at least as high as non-SRI portfolios.[178]

One potential explanation for these counter-intuitive results is that socially irresponsible behavior itself may endanger future profitability. This phenomenon is illustrated by recent comments from Scott Wallace, co-chair of the Wallace Investment Fund:

> We got out five years ago, completely divested from fossil fuels and invested in clean energy solutions, and we're ahead of where we would have been. We've been keeping track of our benchmark of how we were investing. So we're doing better. And it's because the market is starting to understand that all the reserves that are on the books of Exxon and the major oil companies cannot be burned. Their capitalization reflects these huge reserves that are still in the ground, and we're now realizing—the financial analysts are realizing that they can't take them out of the ground. They can't burn them. So the capitalization, the valuation of the companies is dropping. And over the next decade or so, the value of the stocks will continue to plummet, and the value of the alternatives—solar and wind—now competitive with oil and gas, will make those stocks more valuable.[179]

In other words, the consequences of continuing to extract fossil fuels are so dire that regulatory action or the exigencies of climate change will lead to the fossil fuel assets being stranded. Stock prices can be driven down when the market recognizes a company has been acting irresponsibly.[180] So a portfolio that has already divested will outperform an amoral portfolio in these circumstances, essentially avoiding a loss by properly recognizing and pric-

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tion."); *Heirs of Billionaire Oil Tycoon John D. Rockefeller Join Growing Fossil Fuel Divestment Movement*, DEMOCRACY NOW! (Sept. 22, 2014), [hereinafter "DEMOCRACY NOW!"], http://www.democracynow.org/2014/9/22/heirs_of_billionaire_oil_tycoon_john (discussing the Wallace Global Fund's divestment campaign and the resulting increase in returns).

177. Massie, *supra* note 63, 532–34.

178. Rivoli, *supra* note 61, at 272; Humphrey, *supra* note 174.

179. DEMOCRACY NOW!, *supra* note 176.

180. *See* Jeff Frooman, *Socially Irresponsible Behavior and Shareholder Wealth*, 36 BUS. & SOC'Y 221 (1997) (a meta-analysis finding that stock prices decreased upon the market learning of socially irresponsible and illegal behavior).

ing in the costs of irresponsible behavior before the rest of the market.

Another potential explanation for strong investment performance despite SRI constraints is that socially responsible behavior may be a proxy for good management, which can lead to greater profitability.[181] Responsible firms may benefit from "reduce[d] costs and increase[d] productivity by fostering alignment between corporate goals and employee motivations," "minimize[d] transaction costs and potential conflicts with stakeholders," reduced risks from consumer activism and litigation, and increased sales to ethically responsible consumers.[182] One study found that firms with superior CSR performance face lower capital constraints due to greater stakeholder engagement and better transparency.[183]

The literature on the subject is not unanimous. Some studies suggest that the impact of socially responsible behavior is highly industry-specific[184] or dependent on the individual circumstances of the company.[185] Other studies suggest that divestment and negative screening may result in lower returns for the portfolio.[186] The studies on the impact on returns of investing according to ethical guidelines are, ultimately, inconclusive.[187] At the very least, it is not a foregone conclusion that divesting will result in lower returns.

A more definite concern to the investor would be exposing her portfolio to higher risk. Modern portfolio theory holds that diversification—holding stock in a large number of companies across industries—can be used to eliminate company-specific risk.[188] Removing certain companies from the pool of available investments

181. Elaine Pofeldt, *Skip Meat and Donate, or Divest Shares of Exxon?*, CNBC.COM (Oct. 10, 2013, 11:46 PM), http://www.cnbc.com/id/101100227; KINDER, *supra* note 63, at 34.

182. Leonardo Becchetti et al., *Corporate Social Responsibility and Shareholder's Value*, 65 J. BUS. RES. 1628, 1629 (2012).

183. Beiting Cheng et al., *Corporate Social Responsibility and Access to Finance*, 35 J. STRATEGIC MGMT. 1 (2014).

184. LANDIER & NAIR, *supra* note 11, at 84.

185. *Id.* at 78.

186. *See, e.g.*, SOULE, *supra* note 4, at 84; Christopher C. Geczy et al., *Investing in Socially Responsible Mutual Funds*, 27–28 (October 2005), http://ssrn.com/abstract=416380; Patrick Geddes, *Do the Investment Math: Building a Carbon-Free Portfolio*, 2 (Aperio Group Working Paper, 2013), https://gofossilfree.org/se/wp-content/uploads/sites/13/2014/07/building_a_carbon_free_portfolio.pdf (2013) The paradox, discussed below, that a successful divestment campaign may result in higher returns for investors in the target company also suggests that socially responsible investors may forego higher returns of their own creation.

187. *See* Geddes, *supra* note 62, at 7.

188. Gilson & Gordon, *supra* note 42, 869 n.17.

may decrease a portfolio's ability to achieve sufficient diversification, resulting in increased risk. In theory at least, socially conscious investors would need to bear higher risk for larger financial return, which may result in lower risk-adjusted returns than an amoral portfolio.[189] Indeed, the analysis of the South Africa-free portfolio referenced above found an increase in volatility and risk in the South Africa-free portfolios.[190] Ultimately, the cost of reduced portfolio diversity is likely to be quite small since there are few targets relative to the universe of stocks.[191] For example, a study done by the Aperio Group found that a portfolio that excluded the "Filthy Fifteen"—the fifteen U.S. companies judged to be the most harmful in terms of coal use and other metrics—exhibited only a 0.0006% increase in absolute portfolio risk.[192]

Since diversification requires exposure to a broad swath of industries to minimize company-specific risk, the increase in risk may be more significant for campaigns that target an entire industry,[193] such as the 350.org campaign targeting fossil fuel companies. In theory, as an investor chooses to screen out more companies and industries, one would expect non-systemic (idiosyncratic) risk to increase. However, empirical studies have not found support for this theory. The Aperio Group study found that excluding the entire oil, gas, & consumable fuels industry would increase absolute portfolio risk by only 0.0101%.[194] Another study found that portfolios which screened "sin stocks" would not sacrifice in terms of risk or return.[195] As such, if a screened portfolio is carefully constructed, the increase in risk may be miniscule.[196] Thus, there are minimal costs to the investor for divesting, and those that do exist can be addressed by implementing the divestment mechanism carefully.

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189. Christian Gollier & Sebastien Pouget, *"The Washing Machine": Investment Strategies and Corporate Behavior with Socially Responsible Investors*, 7 (IDEI, Working Paper No. 813, Jan. 2014), http://idei.fr/doc/wp/2014/wp_idei_813.pdf.

190. Massie, *supra* note 63, at 534.

191. Harrison Hong & Marcin Kacperczyk, *The Price of Sin: The Effects of Social Norms on Markets*, 93 J. FIN. ECON. 15, 16 (2009) (noting that the cost of being able to diversify is likely to be small even for portfolios screening all "sin stocks" (tobacco, alcohol, and gambling stocks)).

192. Geddes, *supra* note 186, at 3.

193. LANDIER & NAIR, *supra* note 11, at 59–61.

194. Geddes, *supra* note 186, at 4.

195. Humphrey, *supra* note 174.

196. *See* Geddes, *supra* note 62, at 16; LANDIER & NAIR, *supra* note 11, at 64–69.

2. Engagement

Engagement poses a different set of costs from divestment. For activists seeking to submit proposals as part of the campaign, Rule 14a-8 of the Securities and Exchange Act regulations imposes particular requirements:

- the shareholder must hold at least $2,000 worth of stock or at least one percent of the outstanding stock;[197]
- the shareholder must have held this amount continuously for at least a year prior to submission and continue to hold through the date of the meeting at which the proposal is voted on;[198]
- for a regularly scheduled annual meeting, the proposal must be submitted to the company at least 120 days ahead of the meeting;[199]
- the shareholder submitting the proposal, or his representative, must attend the shareholder meeting to present his proposal in person;[200]
- a shareholder may only submit one resolution per year[201] and, if the measure fails to garner at least three percent of the shareholder vote, it may be excluded from proposals in meetings held over the following three years.[202]

If the shareholder fails to follow these ownership or procedural requirements, the company is permitted to exclude her proposal.[203] These ownership, submission, and timeframe requirements make it impossible for an activist to jump quickly in and out of shareholding in order to target a corporation with a stinging proposal or harass them with successive proposals.

Upon submission, the proposal is subject to challenge based on its substance. Rule 14a-8 lists thirteen different substantive reasons for exclusion.[204] These substantive requirements are often used by management to exclude proposals that they oppose, lead-

197. 17 C.F.R. § 240.14a-8(b)(1) (2016).
198. *Id.*
199. 17 C.F.R. § 240.14a-8(e)(2) (2016).
200. 17 C.F.R. § 240.14a-8(h)(1) (2016).
201. 17 C.F.R. § 240.14a-8(c) (2016).
202. 17 C.F.R. § 240.14a-8(i)(12) (2016). The proposal may also be excluded over the next three years if it has been proposed twice in the preceding five years and failed to achieve six percent support both times, or if it has been proposed three times in the preceding five years and failed to achieve ten percent support each time.
203. 17 C.F.R. § 240.14a-8(f)(1) (2016); 17 C.F.R. § 240.14a-8(h)(3) (2016).
204. 17 C.F.R. § 240.14a-8(i) (2016).

ing to much litigation and negotiation with the SEC.[205] The company's management is permitted to include a statement of opposition explaining why shareholders should vote against the proposal in the proxy materials.[206]

Compared to standard external pressure tactics and divestment, the shareholder proposal mechanism requires a relatively high level of commitment and engagement with the target corporation. For an activist who only purchases enough shares to satisfy the Rule 14a-8 requirements, the primary cost would only be the opportunity costs of owning $2,000 worth of shares. For an investor who has a larger stake, such as an institutional investor, the inability to sell for the duration of the campaign may be a more significant cost.

Holding the stock may be costly where the objectionable behavior of the company itself creates additional risk through potential litigation, enhanced regulation, or reputational harms. BP provides an extreme example. A coalition of pension and responsible investment funds submitted a shareholder proposal to be voted on at the April 2010 shareholder meeting.[207] The proposal asked BP to report on the financial, social, and environmental risks associated with its development of Canadian tar sands.[208] At the meeting on April 15, 2010, the proposal received support from 15% of shareholders.[209] Five days later, the Deepwater Horizon oil rig exploded in the Gulf of Mexico, triggering the single largest accidental oil spill in history.[210] BP's share price tumbled 50% over the next two months and has yet to recover to pre-spill levels.[211] Unless the responsible shareholders sold immediately after filing the resolution, their investments lost significant value due to the very type of irresponsible behavior they were decrying.

Another risk activist shareholders face is that their campaign itself may drive the value of the company's shares down, hurting

205. *See, e.g.*, Schwab & Thomas, *supra* note 41, at 1049–51.

206. 17 C.F.R. § 240.14a-8(m)(1) (2016).

207. Press Release, Bos. Common Asset Mgmt., North American Investors Support BP Oil Sands Resolution (Apr. 8, 2010), http://www.bostoncommonasset.com/news/documents/BostonCommonFairPensionsPressReleaseFinal.pdf.

208. *Id.*

209. Danny Bradbury, *BP Shrugs Off Anti-Tar Sands Shareholder Resolution,* BUSINESSGREEN (Apr. 16, 2010), http://www.businessgreen.com/bg/news/1806328/bp-shrugs-anti-tar-sands-shareholder-resolution.

210. Campbell Robertson & Clifford Krauss, *Gulf Spill Is the Largest of Its Kind, Scientists Say*, N.Y. TIMES, Aug. 2, 2010.

211. *See BP P.L.C. (NYSE: BP),* N.Y. STOCK EXCH., https://www.nyse.com/quote/XNYS:BP (last visited Feb. 14, 2016).

their investment. If the campaign is successful at generating publicity around the issue, it may amplify concerns about the risks involved, lowering the market perception of the stock's value.[212] Investment losses may be further increased if the campaign itself imposes significant direct costs on the company in responding to the campaign, decreasing its profitability.[213] Therefore, the activist investor faces the converse of a free rider problem—the root of her influence, the ability to impose costs on the company,[214] may cost the investor in terms of lost value. On the other hand, if the campaign is ultimately successful in achieving reform, the financial performance and perception of the company may be improved[215] and the investor can capture the subsequent increase in the value of her investment.[216]

These changes in value would likely be subsumed by other factors affecting the value of the company, such as economy- and industry-wide trends, changes in the operating environment, and earnings announcements. Thus it is difficult to generalize about the costs borne by the investor in holding the stock itself.

Engagement clearly imposes costs on the activist in terms of the time and effort involved in conducting the campaign. Even merely voting proxies in a conscientious manner can impose significant costs in terms of researching the issue, understanding the proposal, and making a decision.[217] In the case of direct negotiations with management, the activist will expend time and effort to engage.[218] To introduce a shareholder resolution, the activist investor will need to bear the costs of formulating the resolution, submitting

212. *See infra* Part IV.C.

213. *See infra* Part IV.B.2.

214. *See id.*

215. One empirical study found that successful engagements on corporate social responsibility and environmental/social issues generated positive abnormal returns. Elroy Dimson et al., *Active Ownership*, 28 REV. FIN. STUDIES 3225 (2015), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2154724.

216. Christian Gollier and Sebastien Pouget describe the theoretical operation of such a campaign and suggest that it may be a viable investment strategy for a large investor with a long-term investment horizon and credible social orientation. Gollier & Pouget, *supra* note 189.

217. *See* Garrett M. Graham, *Social Investing*, HARVARD MAGAZINE (July–Aug. 2003), http://harvardmagazine.com/2003/07/social-investing.html (describing the process by which Harvard's endowment reaches voting decisions on proxy proposals).

218. *See generally* Nickolay Gantchev, *The Costs of Shareholder Activism: Evidence from a Sequential Decision Model*, 107 J. FIN. ECON. 610, 610–14 (2013) (describing costs involved in shareholder activism in the context of shareholder value maximization).

it to the company, and attending the annual meeting. If the company leadership wrongfully excludes the resolution, the activist must be willing to bear the cost of litigation to ensure that the proposal is included.[219] In the (unlikely) event that the proposal receives majority support, and if management elects not to implement the reform, then the activist shareholder may need to escalate her campaign into a "Vote No" campaign in order to pressure management into enacting the reform.[220] Engagement is costly in terms of time and effort.[221] In terms of money, research on the costs of profit-motivated shareholder activism finds that the average cost of demand negotiations, board representation, and the proxy contest is $10.7 million.[222]

Unlike the uncertain costs of divestment, the costs of an engagement approach are more definite; thus, an engagement approach may raise more concerns for fund managers who are managing investments on behalf of their investors. The Employee Retirement Income Security Act of 1974 (ERISA) governs private pension plans in the U.S.[223] It places restrictions on the manner in which plan managers may invest, including that assets "shall be held for the exclusive purposes of providing benefits to participants in the plan."[224] Public pension funds, bank trusts and mutual funds are subject to similar fiduciary standards requiring managers to put beneficiaries' interests above their own.[225] Asset managers tend to interpret these standards to mean that they must concentrate on quantifiable economic benefits for their beneficiaries.[226] These standards, along with compensation based on short-term performance, tend to focus fund managers' attention on short-term returns, making it less likely they will bear costs in order to reap the long-

219. Keir Gumbs & Daniel Alterbaum, *Using the Courts To Resolve Shareholder Disputes*, INSIGHTS, Apr. 2014, at 9, 12, https://www.cov.com/-/media/files/corporate/publications/2015/04/using_the_courts_to_resolve_shareholder_proposals_disputes.pdf.

220. *See generally* Brownstein & Kirman, *supra* note 125.

221. Richardson, *supra* note 15, at 136.

222. Gantchev, *supra* note 218, at 624.

223. Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. §§ 1001 et. seq.

224. 29 U.S.C. § 1103(c)(1).

225. *See* Bernard S. Black, *Agents Watching Agents: The Promise of Institutional Investor Voice*, 39 UCLA L. REV. 811, 856 (1992).

226. Simon C. Y. Wong, *Why Stewardship Is Proving Elusive for Institutional Investors*, BUTTERWORTHS J. INT'L BANKING & FIN. L. 406, 408–09 (July–Aug. 2010).

term rewards offered by more responsible corporate behavior.[227] Furthermore, whatever gains the responsible behavior may offer would be contingent[228] and difficult to quantify,[229] making expenditures harder to justify. Beneficiaries who object to the use of the fund's stockholding for the sake of furthering a social agenda would be on firmer legal ground to challenge engagement efforts by pointing to quantifiable damages, as compared to divestment actions.

3. Monitoring Costs

Both divestment and shareholder engagement would require the activist to bear the cost of research at the stage of campaign initiation: the time and effort to characterize the issue of concern, develop performance criteria, investigate how companies are performing, and identify targets. On an ongoing basis, the divestor may feel less concerned with monitoring a company's behavior once she has disassociated. After she has loudly taken the "Wall Street Walk," she may feel less concerned with looking back. However, divestors should properly be engaging in ongoing monitoring. To the extent that divestment imposes costs on a corporation, an investor concerned with altering corporate behavior should incentivize reform by re-investing if and when a company changes its practices. A divestor should announce that she is re-investing just as loudly as she announced the divestment and welcome the company back to the fold. The literature suggests that this rarely, if ever, happens: divestment is all stick, no carrot.

Shareholders pursuing engagement do not enjoy the luxury of disassociating themselves from the rogue company. Divestors can choose to ignore the company while, by virtue of their association with a company, activist shareholders would feel more compelled to continually monitor the behavior of a corporate actor. Beyond that practical reality, there is a qualitative difference in the monitoring that an activist shareholder must undertake. Divestment proposes a compliance/non-compliance binary: if the company is in compliance, it is worthy of investment; if it fails to comply, then it is out of the portfolio. Shareholder engagement, on the other hand, necessarily involves more nuance since it requires proposing reforms and engaging with the company to find common ground.

227. *Id.* at 406–09; Jay Youngdahl, *The Time Has Come for a Sustainable Theory of Fiduciary Duty in Investment*, 29 HOFSTRA LABOR & EMPLOYMENT L. J. 115, 121–33 (2011).

228. Gordon & Gilson, *supra* note 42, 891–92.

229. Dimson et al., *supra* note 54, at 18.

Where a specific policy is recommended via shareholder resolution or informal engagement, monitoring will be required to understand whether the policy is being implemented properly.[230] As an illustration, in 2004, religious groups and a Service Employees International United fund sponsored a shareholder resolution calling on Coca-Cola to produce a report on best practices and managing business risks associated with HIV/AIDS, tuberculosis, and malaria.[231] In the lead-up to submitting the resolution, the activists met with company staff and members of the Coca-Cola Africa Foundation over the course of two years.[232] As a result, the proposal received the support of the Coca-Cola board of directors and passed with ninety-seven percent support among shareholders.[233] However, when Coca-Cola issued the report, it focused solely on Coke's HIV/AIDS initiatives in Africa.[234] In response, the activists published a letter praising Coke for its efforts, but pointing out the shortcomings of the report.[235] In this example, engagement required discussions with management, drafting and submitting a proposal, analyzing the result, and responding to the company's efforts.

Shareholder engagement, by virtue of its ability to give nuanced guidance in an iterative, collaborative process, makes monitoring the company's responses more complex and resource-intensive. One study in the context of profit-motivated activism found that monitoring costs reduced the activist's abnormal returns by more than two-thirds.[236] Having a say in the direction of a company provides greater nuance to an engagement approach, but that nuance comes at a price.

B. Direct Costs Imposed on Target Company

The basic goal of anti-corporate protest tactics is to raise the costs of engaging in problematic behavior.[237] The imposed costs

230. Carleton et al., *supra* note 151, at 1339.

231. Foster, *supra* note 148, at 194–95.

232. Barry B. Burr, *Coca-Cola Proposal Endorsement May Have Domino Effect Elsewhere*, PENSIONS & INVESTMENTS (March 22, 2004), http://www.pionline.com/article/20040322/PRINT/403220713/coca-cola-proposal-endorsement-may-have-domino-effect-elsewhere.

233. *Id.*; Foster, *supra* note 231, at 195.

234. Foster, *supra* note 231, at 196.

235. *Id.*

236. Gantchev, *supra* note 218, at 629.

237. *See* Brayden G. King, *The Tactical Disruptiveness of Social Movements: Sources of Market and Mediated Disruption in Corporate Boycotts*, 58 SOC. PROB. 491, 491–92 (2011) (discussing costs to corporations in terms of "disruption"); *see also* den

can be direct—the tactic hurts the bottom line by raising costs or decreasing profit—or indirect—the company must bear costs of reacting to the fallout from the tactic or suffer from a loss of reputation.[238] By impacting corporate financial performance, activists can incentivize socially beneficial behavior.[239] If the activist campaign stands to impose higher costs on the company than the costs of taking the requested action, it makes good business sense to take the action. Management may also consider the reputational damage that they will suffer as a result of missing earnings benchmarks.[240] The higher the costs that a campaign imposes on the target, the more likely it is to bring about change.[241] These costs act as an incentive to take the concerns of social movements seriously.[242]

This mode of influence may also be stated in terms of resource dependence: "When stakeholders control access to some needed resource, the stakeholders have the ability to put those resources at risk and thereby endanger the firm's survival."[243] In this case, the needed resource is investment capital to fund a company's growth. Secondary stakeholders (activist groups) may increase their relevance to corporate decision makers by exerting control over a needed resource.[244]

1. Direct Costs Imposed by Divestment Are Attenuated

The capacity for divestment to impose direct costs on a corporation is questionable. It seems intuitive that, by triggering a boycott of capital, a divestment campaign could make it more difficult for a company to raise funds. Some proponents of divestment voice this sentiment by making reference to "rais[ing] the cost of capital" for

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Hond & de Bakker, *supra* note 33, at 909–11. Den Hond and de Bakker discuss both a "logic of material damage" and a "logic of numbers," but it is clear from their discussion that "numbers" are a means to achieve the intended outcome: "damage."

238. *See* den Hond & de Bakker, *supra* note 33, at 909–10 (discussing costs in terms of material and symbolic damage).

239. Soule, *supra* note 4, at 78.

240. John R. Graham et al., *The Economic Implications of Corporate Financial Reporting*, 40 J. Acct. & Econ. 3, 28 (2005).

241. Charles Eesley & Michael J. Lenox, *Firm Responses to Secondary Stakeholder Action*, 27 Strat. Mgmt. J. 764, 777 (2006).

242. *See* King & Soule, *supra* note 31, at 437.

243. Brayden King, *A Social Movement Perspective of Stakeholder Collective Action and Influence*, 47 Bus. & Soc. 21, 24 (2007).

244. *See id.*

irresponsible corporations[245] or theorizing that a successful divestment campaign will result in a drop in share prices.[246] Others simply refer to "raising the price" of the problematic behavior without specifying how these costs will be imposed.[247] Hirschman's characterization of "exit" as an economic mechanism, relying on free-market forces to work change,[248] seems to provide a theoretical underpinning for this intuition. However, the view of "exit" in standard product markets is maladapted to understanding divestment of a company's stock.

A boycott of capital seems analogous to other boycotts that have a theoretical basis for imposing costs on a target. Selling stock or refusing to buy new shares resembles a consumer boycott: a boycott by purchasers of stock. A consumer boycott operates, in part, by reducing sales of a target's products, thereby reducing revenue or increasing marketing costs,[249] and thus reducing the target's profit.

Applying the logic of a consumer boycott suggests that a company would have to charge a lower price for its stock in order to sell all the issued stock or offer more value (in terms of voting rights, dividends, or convertibility) in order to raise the same amount of money. Regardless of the mechanism, the company's bottom line would be hurt as a direct result of a divestment campaign that lowers its stock price. A lower stock price may hinder a company's ability to acquire other companies using stock as consideration[250] and may make the company more vulnerable to takeover bids.[251] A lower stock price will also adversely affect executives' compensation, which is often tied to the company's share price performance.[252] Value-maximizing managers would choose to implement a change that is not cost-justified on its own where the concomitant higher costs of capital resulting from divestment offset the net cost of compliance.[253]

However, capital markets do not function like product markets. Modern corporate finance theory suggests that the demand

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245. Dimitri Lascaris, Toronto 350.org, *Divestment Brief Presentation to the University of Toronto President* (Mar. 6, 2014), http://www.toronto350.org/presentation.

246. Voorhes, *supra* note 60, at 134–35.

247. BARGHOUTI, *supra* note 6, at 18.

248. *See* HIRSCHMAN, *supra* note 47, at 19.

249. *See* King, *supra* note 237, at 494.

250. *See* LANDIER & NAIR, *supra* note 11, at 43.

251. Jeremy C. Stein, *Takeover Threats and Managerial Myopia*, 96 J. POL. ECON. 61, 62 (1988).

252. LANDIER & NAIR, *supra* note 11, at 43.

253. *Id.*

curve for a company's stock is horizontal.[254] Share price is determined by the present value of the company's future cash flows or, more accurately, the market's perception of that value.[255] In other words, a decrease in demand would not significantly depress stock prices. Even the sale of a large stake in a company will only lead to a temporary drop in share prices: if a share price becomes undervalued in relation to the future cash flows of the company, unconstrained investors will scoop up the stocks and return the price to its value-justified level.[256] The market for the exchange-traded securities of public companies is highly liquid, so a divestment push would not impose costs for searching out new purchasers or suppliers like a consumer or supplier boycott of commercial goods.[257] As long as there are enough indifferent investors in the market to maintain liquidity, a divestment effort is unlikely to have an impact on the share price of a company even with significant buy-in from investors. Hirschman seems to anticipate this shortcoming of the "exit" approach: "[I]f demand is highly inelastic . . . losses will be quite small and the firm will not get the message that something is amiss."[258]

There are some theoretical limits to the assumptions in the above scenario. The above description would be accurate for the individual investor considering divesting. However, the capital asset pricing model relies on an assumption that all investors in the market are fully diversified.[259] If this assumption were relaxed in order to account for a group of socially responsible investors who are not diversified as a result of avoiding certain stocks, then investors in an irresponsible company's stock will bear firm-specific risk and therefore require higher rates of return to hold the stock, which depresses stock prices.[260] This suggests that the fewer investors available to purchase a given security, the greater the decline in

254. M. Todd Henderson, *Divestment and Financial* Illiteracy, HUFFINGTON POST (May 21, 2013), http://www.huffingtonpost.com/m-todd-henderson/divestment-and-financial-_b_3308747.html.

255. *See, e.g.*, Becchetti et al., *supra* note 182, at 1629.

256. Henderson, *supra* note 254; SIMON ET AL., *supra* note 68, at 53.

257. This assumption may not hold for smaller, non-public companies.

258. Hirschman, *supra* note 47, at 24.

259. Rivoli, *supra* note 61, at 278. Rivoli also notes that the ideal capital market may not exist, and thus the demand curve will slope downward in cases where investors "do not recognize close substitutes for the shares of a firm" or where transaction costs decrease liquidity. *Id.*

260. *Id.*, at 278–79.

price will be.[261] A restricted investor base may result in a higher cost of capital to the company.[262]

There is a paucity of empirical research on the effects of divestment on the share price of target companies. One study lends some empirical support to the theoretical shortcomings of divestment's ability to affect share price in the context of the anti-Apartheid movement,[263] which is widely considered the most successful divestment campaign to date.[264] The study examined the share prices of companies doing business in South Africa during the divestment campaign.[265] The researchers found little discernible effect in the companies' share prices upon the announcement by institutional investors that they would be divesting from those companies.[266] Further, once those companies stopped operating in South Africa, there was no discernible increase in their share prices.[267] Lending anecdotal support for this finding, interviews with the target companies' executives reveal that they did not feel pressure from falling stock prices even at the height of the divestment campaign.[268]

Research on the effects of SRI on stock price suggests that negative screening can lower stock price if a critical mass of investors screens out a certain company. As explained above, selling a stock or refusing to purchase a stock as an act of socially responsible investing designed to impact a company's behavior are indistinguishable from explicit acts of divestment. So the literature studying the effects of SRI on stock price can help explain the effects that a successful divestment campaign might have. One theoretical study posits that 20% of investable capital would need to eschew environmentally irresponsible companies in order to exert noticeable downward pressure on their stock prices.[269] In another study, Hong and Kacperczyck undertook a survey of data from 1965 to 2006 of the valuation and returns of "sin stocks," the stocks of companies profiting from alcohol, gambling, and tobacco that are screened out from most of the largest ethical investing funds.[270] Their analysis found that the "sin stocks" were under-valued relative to compa-

261. *Id.*, at 279.

262. *Id.*

263. *See* Teoh et al., *supra* note 78.

264. *Supra* note 100.

265. Teoh et al., *supra* note 98, at 35–36.

266. *Id.* at 35.

267. *Id.*

268. Voorhes, *supra* note 60, at 130, 138, 138 n.22.

269. Heinkel et al., *The Effect of Green Investment on Corporate Behavior*, 36 J. FIN. & QUANTITATIVE ANALYSIS 4 431, 447 (2001).

270. Hong & Kacperczyk, *supra* note 191, at 17.

rable "non-sin" stocks by 15–20%.[271] They estimated that these differences were generated by 10–15% of investable dollars screening for sin stocks.[272] Two event studies found a significant negative effect on companies' stock price resulting from removal from one of the prominent social investing indices.[273] These studies did not specifically calculate the amount of capital employing screens based on these indices, but both mentioned that one in nine (11%) invested dollars are in socially responsible portfolios.[274] Based on existing research, it is unclear precisely what percentage of investors (or, more accurately, what percentage of dollars invested in equities) would need to divest from a stock in order to have a noticeable effect on a publicly traded company.[275] However, it appears that downward effects can be observed once 10–20% of capital eschews a particular stock. In theory, the effect would become more pronounced as the percentage increases past that threshold.[276]

It is important to emphasize that these percentages refer to the entire universe of investable capital and not just to the investors in a given company. Convincing more than 10% of the shares in a publicly traded company to divest would be an impressive feat, but there would be sufficient demand in the market to absorb the sold stock without anything more than a temporary drop in share price. If a divestment advocate hopes to exert financial pressure on the target company, her job is much more daunting: she must convince the threshold percentage, estimated at 10–20%, of the entire market for corporate equities, to avoid the stock. This would include any international investors who would purchase U.S. securities if they were underpriced relative to their fundamental value.

271. *Id.*

272. *Id.* at 32. The proportion of ethical investors needed to affect returns is dependent on the number of stocks that are excluded by these ethical investors. In this study, sin stocks represented about 5% of the market. *Id.*

273. Jonathan P. Doh et al., *Does the Market Respond to an Endorsement of Social Responsibility? The Role of Institutions, Information, and Legitimacy*, 36 J. MGMT. 1461, 1480 (2010) (analyzing Calvert Social Fund); Becchetti et al., *supra* note 182, at 1635 (analyzing the Domini 400 Social Index).

274. Doh et al., *supra* note 273, at 1462; Becchetti et al., *supra* note 182, at 1628.

275. Richardson, *supra* note 15, at 135.

276. Rivoli, *supra* note 61, at 277–80 ("In summary, although perfect markets assumptions preclude the theoretical possibility that SRI will 'make a difference,' a significant volume of theoretical finance research suggests that SRI may indeed be expected to affect corporate behavior when certain unrealistic assumptions are relaxed. When these assumptions are relaxed, theory predicts that the size of the firm's investor base will affect prices and returns.").

Establishing that there is some threshold percentage of ethical capital which would exert downward pressure on share price raises another question: is there a sufficient amount of capital that is a viable target for divestment to reach that threshold? As a baseline, we can look at the amount of capital that is already employing ethical screens or engaging in shareholder engagement, suggesting that it would be responsive to a divestment message. At the start of 2014, $6.57 trillion of the $36.8 trillion under management in the United States was invested according to socially responsible guidelines, representing nearly 18% of U.S. assets under management.[277] The proportion of ethically invested assets has grown by 13% per year since 1995, representing a tenfold increase from 1995 to 2014.[278] SRI analysts expect the proportion to continue to increase in the coming years.[279] Worldwide, the appetite for responsible investment is even larger. The United Nations-supported Principles for Responsible Investment (PRI), a set of principles designed to incorporate environmental, social, and governance (ESG) issues into investment analysis and ownership practices, had 1380 signatories representing $59 trillion in assets under management in 2015,[280] compared to global assets under management of over $74 trillion.[281] PRI is aspirational—it does not require immediate implementation of SRI principles.[282] Further, it is likely that a significant portion of the investors represented by the U.S. SRI figures and worldwide PRI signatories are committed long-term institutional investors who would prefer an engagement approach and thus be durably resistant to a divestment approach. However, the numbers are adequate to suggest that a significant portion of assets under management incorporate or soon will incorporate non-financial criteria into their investment decisions. Thus, a divestment cam-

277. US SIF – The Forum for Sustainable and Responsible Investment in the US, Report on U.S. Sustainable, Responsible and Impact Investing Trends 2014, at 12–13 (2014), http://www.ussif.org/files/publications/sif_trends_14.f.es.pdf.

278. *Id.*

279. Landier & Nair, *supra* note 11, at 94.

280. *About the PRI*, Principles for Responsible Investment, http://www.unpri.org/about-pri/about-pri/ (last visited Nov. 11, 2015). It should be noted that the PRI initiative incorporates corporate governance standards, making it more likely that some number of signatories are motivated by purely financial goals.

281. Gary Shub et al., *Global Asset Management 2015: Sparking Growth with Go-to-Market Excellence*, bcg.perspectives (July 7, 2015), https://www.bcgperspectives.com/content/articles/financial-institutions-global-asset-management-2015-sparking-growth-through-go-to-market-strategy/.

282. *About the PRI*, *supra* note 280.

paign may approach the required threshold of support without needing to convert purely financial investors to ethical investors.

Aside from the aggregate amounts of capital that employ SRI principles in investment, a closer look at the types of institutional investors that own U.S. corporate equities is helpful to understanding whether a divestment campaign could achieve sufficient support to depress stock prices. Hong and Kacperczyk identify factors that could subject an institution to social norm pressure: "[P]ositions in stocks are public information, institutions with diverse constituents, and institutions that can be readily exposed to public scrutiny (e.g., picketing by an unhappy minority)."[283]

The endowments of non-profit organizations are the most visible target for divestment. Non-profit organizations, when organized as 501(c)(3) charitable organizations, may only be operated for public purposes.[284] Moreover, the endowments of universities, churches, and non-profit organizations are funded by charitable donations; the donors are loathe to see their charitable funds financing causes that they do not believe in themselves.[285] Universities are a flashpoint for divestment due to passionate student groups and rich endowments.[286] As a result of the anti-Apartheid movement, forty-three educational institutions divested from companies doing business in South Africa.[287] Today, university campuses are a major target of 350.org's Fossil Free divestment campaign; as of February 2016 fifty-eight colleges and universities had committed to pursuing divestment.[288] One hundred thirty-six religious institutions and 126 foundations had also signed on.[289]

Public pension funds present another likely target for divestment efforts. Since public pensions funds are governmental (or quasi-governmental) institutions, they are more transparent and

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283. Hong & Kacperczyk, *supra* note 191, at 16. Their study found lower incidences of ownership of sin stocks among institutional investors. *Id.* at 24.

284. *Exemption Requirements - 501(c)(3) Organizations*, IRS.GOV, https://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/Exemption-Requirements-Section-501(c)(3)-Organizations (last visited Apr. 16, 2016).

285. LANDIER & NAIR, *supra* note 11, at 19.

286. A 2015 study of 812 colleges and university endowments estimated their holdings at $529 billion. Press Release, NACUBO & Commonfund Institute, Educational Endowments' Investment Returns Decline Sharply to 2.4% in FY2015; 10-Year Returns Fall to 6.3%, (Jan. 27, 2016), http://www.nacubo.org/Documents/2015%20NCSE%20Press%20Release%20%20FINAL.pdf.

287. LANDIER & NAIR, *supra* note 11, at 20 (quoting JOHN C. HARRINGTON, INVESTING WITH YOUR CONSCIENCE 34 (2002)).

288. *Divestment Commitments*, FOSSIL FREE, http://gofossilfree.org/commitments/ (last visited Feb. 15, 2016).

289. *Id.*

susceptible to political pressure than private funds.[290] In the United States, the persons responsible for managing state and local pension funds, comptrollers or trustees, are often elected or appointed to those positions.[291] A public fund manager's investment approach can become an election issue.[292] For example, the successful 2013 candidate for New York City Comptroller, the position responsible for city workers' pension funds, promised to prioritize environmental sustainability as a factor for investing.[293] Government retirement funds control 8% of the corporate equity market.[294]

Not surprisingly, these funds are targeted by divestment campaigns with considerable success. In the 1980s, thirty-eight state or city governments adopted partial or full divestment policies for companies doing business in South Africa.[295] As of February 2016, sixty-two government entities had committed to pursue divestment at the urging of the 350.org Fossil Free campaign.[296] Similarly, sovereign wealth from abroad is subject to many of the same pressures. For example, Norway's Government Pension Fund is seen as a pioneer in ethical investment practices, with a mandate to avoid investments that could contribute to unethical acts or omissions, such as serious violations of human rights, gross corruption, severe environmental damages, or violations of fundamental ethical norms.[297]

Private retirement funds provided by companies to their employees own 9% of the corporate equity market[298] and present a more complicated picture. There are two main types of private retirement plans: defined benefit plans and defined contribution plans. Defined benefit plans promise beneficiaries a fixed payment over time.[299] Such plans place the investment risk on the company[300] and place fiduciary obligations on plan managers to man-

290. Sanford M. Jacoby, *Convergence by Design: The Case of Calpers in Japan*, 55 AM. J. COMP. L. 239, 289 (2007).

291. *See* Marcel Kahan & Edward B. Rock, *Hedge Funds in Corporate Governance and Corporate Control*, 155 U. PA. L. REV. 1021, 1059–60 (2007).

292. *Id.*

293. Leanna Orr, *NYC Comptroller Candidate Vows ESG-Aware Pensions*, CHIEF INV. OFFICER (Aug. 26, 2013), http://www.ai-cio.com/channel/newsmakers/nyc_comptroller_candidate_vows_esg-aware_pensions.html?terms=esg.

294. GOLDMAN SACHS, AN EQUITY INVESTOR'S GUIDE TO THE FLOW OF FUNDS ACCOUNTS 4 (2013), http://www.btinvest.com.sg/system/assets/12141/Goldman%20Sachs%20-%20US%20Strategy%202013%20Mar%2011%20GS.pdf.

295. Voorhes, *supra* note 60, at 135.

296. *Divestment Commitments*, *supra* note 288.

297. Chesterman, *supra* note 61, at 590.

298. GOLDMAN SACHS, *supra* note 294, at 590.

299. Gilson & Gordon, *supra* note 42, at 881.

300. *Id.*

age the investments on behalf of the employee beneficiaries.[301] Thus, we would expect investment managers of defined contribution plans to be resistant to considering non-financial objectives in managing their investments.

In defined contribution plans, on the other hand, the company only promises to contribute a certain amount to the employee's account and the employee chooses the investments and bears the investment risk.[302] In recent years, defined benefit plans have been significantly displaced by defined contribution plans.[303] This trend favors shareholder activist campaigners, since individuals acting as their own investment managers will not be constrained in their investment decisions compared with fiduciaries managing accounts on their behalf. On the other hand, individuals are widely dispersed as compared to centralized management and are not required to disclose their holdings, which may make targeting them more challenging.

The trend towards defined contribution plans has helped speed the rise of another type of institutional investor: the mutual fund.[304] Mutual funds provide a low-cost, straightforward means for individual investors to achieve a diversified portfolio[305] and have come to account for 20% of the ownership of U.S. corporate equity.[306] In the past, mutual fund ownership of equities would have been seen as a natural barrier to shareholder campaigns, since part of their attractiveness depends on providing diversification and keeping costs low. However, investment funds engaged in SRI have exploded in recent years, going from fifty-five investment funds with assets of $12 billion in 1995 to 925 investment funds with assets of $4.3 trillion in 2014.[307] In 2003, the SEC adopted a rule requiring mutual funds to disclose their proxy votes, subjecting them to increased scrutiny by activist shareholders.[308] Now, if an investor wants to exclude a certain company, industry, or practice, there is

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301. *See discussion infra* Part III.A.2 regarding fiduciary duties of investment managers.

302. Gilson & Gordon, *supra* note 42, at 881.

303. *Id.* at 882.

304. *Id.* at 883–86.

305. *Id.* at 884–86.

306. GOLDMAN SACHS, *supra* note 294.

307. U.S. SIF, *supra* note 277, at 13. These figures include mutual funds, variable annuity funds, closed-end funds, exchange-traded funds, alternative investment funds and other pooled products.

308. Jonathan D. Glater, *S.E.C. Adopts New Rules for Lawyers and Funds*, N.Y. TIMES, Jan. 24, 2003, http://www.nytimes.com/2003/01/24/business/sec-adopts-new-rules-for-lawyers-and-funds.html.

likely a mutual fund that will accommodate her desire. If a divestment campaign is successful in creating demand for certain companies or industries to be excluded, more capital will move to funds which meet that demand or new funds will be created that do.[309] Mutual funds no longer act as an absolute bar to divestment.

One segment of the corporate equity market appears to be durably resistant to divestment pressure: hedge funds. Hedge funds represent at least 3% of the U.S. corporate equity market.[310] Hedge funds face much less stringent disclosure requirements than public pension funds or mutual funds[311] and tend to focus on short-term absolute returns.[312] Hedge funds have shown some willingness to consider ESG factors in investing, but only as a means for providing higher returns and/or moderated risk.[313] Effectively, any consideration of factors not related to financial performance would need to be motivated by the investors in the hedge fund.

The above analysis suggests that most constituents of the corporate equity marketplace are susceptible to appeals based on social responsibility, and thus it is theoretically possible that divestment campaigners could achieve sufficient traction to push share prices down. However, there are a few challenges campaigners may face in recruiting new investors to their cause (and preventing defection) that bear consideration. The prospect of divestment decreasing share prices in a company presents a paradoxical challenge: if investors divest in sufficient numbers to drive stock prices down, increasing the cost of capital for the company, then the stock will provide higher returns.[314] This would increase returns for amoral investors who purchase the unacceptable stocks.[315] Hong and Kacperczyk's study provides some empirical support for this paradox: "sin stocks" were significantly under-valued relative to

309. *See* Democracy Now!, *supra* note 174 ("Everybody who owns a 401(k), a pension fund, who is an alumnus of a university that writes a check occasionally, who has any sort of mutual fund investment, you can go to your advisers, you can go to your fund and say, 'I want out of the dirty stuff. I want you to set up a clean energy fund. I want a vehicle where I can express my values consistent with my financial goals.' Everybody can put that kind of pressure.").

310. GOLDMAN SACHS, *supra* note 294.

311. Kahan & Rock, *supra* note 291, at 1062–64; Sara Sjolin, *Hedge Fund Disclosures for SEC Eyes Only*, MARKETWATCH (July 1, 2011), http://www.marketwatch.com/story/hedge-fund-disclosures-for-sec-eyes-only-2011-07-01.

312. Nina Rohrbein, *Hedge Fund Paradox*, INVEST. & PENSIONS EUR. (Mar. 2011), http://www.ipe.com/investment/investing-in/hedge-funds/hedge-fund-paradox/39585.fullarticle.

313. *Id.*

314. Dimson et al., *supra* note 229, at 20.

315. Heinkel et al., *supra* note 269, at 447; Rotternberg, *supra* note 92, 238.

comparable "non-sin" stocks from 1965 to 2006 and thus provided abnormal returns.[316] This phenomenon increases the opportunity cost of divestment, which would incentivize marginal social investors—those who seek to balance investment performance and social outcomes—to remain in the stock (or return to it after selling), all other things being equal. In other words, a divestment campaign that is successful in imposing direct economic costs on a company may create a disincentive for investors to participate.[317]

Divestment campaigners face another challenge in terms of risk: as an investor screens out more stocks, the risks associated with imperfect diversification will increase, as suggested above.[318] As greater numbers of investors implement SRI screens, they may become marginally less willing to divest from additional companies. This phenomenon could present an additional source of inertia for successive divestment campaigns.

Finally, it is worth noting that companies are not continuously selling their stock. A company raises money from stock at the time of issuance; after issuance, changes in share price in the secondary market do not directly impact the corporation's cash flows.[319] A lower stock price may, however, hurt a company's ability to raise money through future issuances of stock.[320] However, companies have recourse to other sources of financing, for example bond issuances, bank loans, or retained earnings. In fact, equity financing makes up only a small part of the mix of corporate financing activity.[321] Bond issuances dwarf stock issuances as a source of corporate

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316. Hong & Kacperczyk, *supra* note 191, at 17. Note that a recent study has called the findings of Hong and Kacperczyk into question. Hampus Adamsson & Andreas G. F. Hoepner, *The 'Price of Sin' Aversion: Ivory Tower Illusion or Real Investable Alpha?* (Sept. 11, 2015), http://ssrn.com/abstract=2659098.

317. This presents another paradox for the activist: given enough time, the increased returns on the tainted stock relative to the rest of the market would have the effect of shifting more wealth into the hands of amoral investors. This macro effect would decrease the proportion of capital in the hands of social investors, making it less likely that social investors would be able to have an impact on stock prices going forward. *See* Heinkel et al., *supra* note 269, at 447.

318. *Supra* Part IV.A.1.

319. *Why Do Companies Care About Their Stock Price?*, INVESTOPEDIA, (Jan. 17, 2014, 8:40 AM), http://www.investopedia.com/articles/basics/03/020703.asp.

320. *Id.*

321. *See, e.g.*, John Schwartz, *Rockefellers, Heirs to an Oil Fortune, Will Divest Charity of Fossil Fuels*, N.Y. TIMES, Sept. 21, 2014, http://www.nytimes.com/2014/09/22/us/heirs-to-an-oil-fortune-join-the-divestment-drive.html ("Donald P. Gould, a trustee and chair of the Pitzer investment committee and president of Gould Asset Management, said that everyone involved in the decision knew that the direct and immediate effect on the companies would be minimal. . . . Even if the movement were to depress share prices, the energy companies, which make enormous profits

financing in the United States. In 2015 the United States saw $256 billion in stock issuance compared to $1.5 trillion in corporate bond issuance.[322] Therefore, if a divestment campaign were able to cause a drop in share price that made equity financing less attractive, management would be able to shift to other forms of financing like debt.

Consistent with this expectation, Hong and Kacperczyk observed higher leverage ratios among sin companies whose stock is subject to ethical screens.[323] The debt market is less transparent than the equity market, so it is more difficult to discern from whom a given company is borrowing and who is purchasing a company's bonds.[324] Without the ability to identify a company's lenders, it will be exceedingly difficult to recruit them into a boycott campaign as a supplier of capital and raise the cost of debt financing.[325] The same obstacle exists when companies receive funding from privately traded alternative investments like hedge funds and private equity.[326] While a company's executives may be sensitive to stock price due to their performance compensation, a marginally lower stock price will not create a significant impediment to a company's operations due to the availability of other forms of financing that are insulated from activist pressure.

In conclusion, the potential audience of investors for a divestment campaign is wide and growing. However, to actually drive a company's stock prices down would take tremendous support among the world's investors. By illustration, even if the Fossil Free campaign were able to convince all the U.S. universities to divest their endowments, that would represent less than one percent of the capitalization of global equity markets,[327] far short of the

from their products, do not need to go to capital markets to raise money, he noted.").

322. SIFMA REPORT, *SIFMA US Quarterly Highlights, 4Q'15*, 2 (Jan. 20, 2016), http://www.sifma.org/research/item.aspx?id=8589958433.

323. Hong & Kacperczyk, *supra* note 191, at 18. They also aptly note that many sin companies may simply choose to remain private because they will be shunned by investors. *Id.*

324. *Id.* at 32.

325. Indeed, with the exception of the Rainforest Action Network's campaign against Mitsubishi discussed in Part I.B.1, this researcher did not come across examples of activists targeting a company's lenders.

326. *See* Matthew Cunningham-Cook, *Why the Fossil Fuel Divestment Movement Is a Farce*, AL JAZEERA AMERICA, July 7, 2014, http://america.aljazeera.com/opinions/2014/7/fossil-fuel-divestmentenvironmentpoliticscollegeenergy.html.

327. Ivo Welch, *Why Divestment Fails*, N.Y. TIMES, May 9, 2014, www.nytimes.com/2014/05/10/opinion/why-divestment-fails.html. As of February 2016, the Fossil Free campaign claims to have received commitments of full or partial divest-

threshold needed to influence stock prices. Even if the equity markets became inhospitable, companies would have alternative means of raising capital that are less susceptible to divestment campaigns. A divestment campaign would need to be several orders of magnitude more successful than even the paradigmatic success story, the anti-apartheid campaign, to impose direct financial costs on the target company. It is possible, but unlikely.

2. Costs Imposed through Engagement

Engagement extracts minor costs from the target company's bottom line. A company must expend resources to add the shareholder's resolution to the proxy ballot and respond to it. One researcher put the costs of determining whether or not to include a shareholder proposal at approximately $46,000, with an additional cost of including the proposal of approximately $63,000.[328] Even these relatively modest estimates have been critiqued as too high.[329] The basic costs of accommodating a shareholder's resolution are insignificant in comparison to the budget of a publicly traded company.[330] However, if the leadership opposes a resolution, they must press their own counter-campaign to dissuade shareholders from supporting it.

The time and effort required of management to respond are significant costs to which company leadership will naturally be sensitive.[331] Company leadership will often agree to an activist shareholder's demands even when it would impose costs on the company and the demand lacks broad support among shareholders. For example, PepsiCo agreed to disclose its lobbying and trade association

ment from institutions valued at $3.4 trillion worldwide, *Divestment Commitments*, *supra* note 288, which represents less than 5% of global assets under management, *cf.* Shub, *supra* note 281.

328. Stephen M. Bainbridge, *A Comment on the SEC's Shareholder Access Proposal*, ENGAGE at 18, 22 (2004) (Bainbridge's estimates have been adjusted for inflation to 2016 dollars).

329. *See* Michael R. Levin, *The Deal Professor's GPA Plummets*, THE ACTIVIST INVESTOR BLOG (Aug. 21, 2014), http://www.theactivistinvestor.com/The_Activist_Investor/Blog/Entries/2014/8/21_The_Deal_Professors_GPA_Declines.html.

330. As a point of illustrative comparison: the median yearly pay for a single director of an S&P 500 company was $255,000 as of October 30, 2015. Theo Francis & Joann S. Lublin, *Corporate Drectors' Pay Ratchets Higher as Risks Grow*, WALL ST. J. (FEB. 24, 2016, 3:29 PM), http://www.wsj.com/articles/corporate-directors-pay-ratchets-higher-as-risks-grow-1456279452.

331. *See* Garrett M. Graff, *Social Investing*, HARVARD MAGAZINE (July–Aug. 2003), http://harvardmagazine.com/2003/07/social-investing.html (quoting Harvard Management Company President Jack Meyer, "Companies would prefer you divest, rather than harass them with proxies as shareholders.").

relationships on the condition that the New York State workers' pension fund withdraw a shareholder resolution on the topic.[332] PepsiCo did this despite the resolution receiving only 7.1% support in a shareholder vote the previous year.[333] The willingness of some companies' leadership to compromise on important issues despite low shareholder support and operational costs suggests that shareholder campaigns inflict real costs on the company, or at least personal costs on management themselves.

It should be noted that this type of "gadfly" approach may present a concern for some fund managers. Fund managers may hope to provide services to the target corporation in other areas, such as managing their pension funds.[334] Pressing a costly engagement campaign may alienate company leadership. Thus, investment managers generally are disinclined to engage in gadfly tactics that could taint their reputation among corporate leaders.[335] The increased responsiveness an activist may expect to achieve by imposing a costly engagement process on management may be offset by decreased buy-in from institutional investors.

C. Indirect Costs and Expressive Impact

Since shareholder tactics have limited ability to project "hard power" by directly impacting the target company's bottom line, the proper aim of shareholder campaigns is to influence corporate leadership by maximizing the expressive impact of their actions. In the context of influencing a company's behavior, the three primary facets of a tactic's expressive impact are its power to raise awareness, persuade, and inflict costs indirectly through reputational harm.

Activists need to raise awareness about their issue and why it is important before they can hope to persuade their audience that their chosen reforms are desirable. Persuasion, in this context, operates to convince corporate leadership that the proposed changes are in the best interests of the corporation. Persuasion operates in a secondary function to recruit other shareholders to join in the campaign and to entice the media to cover their efforts favorably in order to amplify their message.

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332. *Special Report: Public Pension Fund Activism*, PROXY MONITOR (2013), http://www.proxymonitor.org/forms/2013Finding3.aspx.

333. *Id.*

334. Kahan & Rock, *supra* note 291, at 1054–56.

335. *See id.*; *see also* Gerald F. Davis, *A New Finance Capitalism?*, 5 EUR. MGMT. REV. 11, 20 (2008) (examining the correlation between Fidelity's employee benefits management business and proxy voting behavior).

Stakeholders who are unable to inflict direct costs on a company may influence company leadership by imposing reputational costs on the company through bad press.[336] "[T]he reputation of a firm is a kind of intangible asset that can be used to create shareholder value."[337] Since reputation is an asset of the company, harm to that asset will concern investors and company leadership alike since it may endanger the company's ability to carry out its objectives.[338] Contentious tactics may also be a source of new information that investors may use to evaluate the attractiveness of a company as an investment.[339] Activism is most successful when it can signal dissatisfaction among the corporation's stakeholders,[340] in this case its shareholders.

It is important to understand with some clarity the actual goals of activist expression, but since the goals and mechanics of raising awareness, persuasion, and infliction of reputational costs are inextricably linked they will not be treated individually in the following analysis. It is sufficient to understand that achieving these goals is dependent on the modes of communication employed, the frames used, the credibility of the message, and the audience.

1. The Expressive Value of Divestment Is Strictly Symbolic

Engagement requires that an investor maintain an ownership stake, however small, in the target company and thereby maintain an association with the company. Divestment, on the other hand, communicates a cutting of ties between the investor and the target corporation. The cutting of ties is a demonstration that the company's behavior is so condemnable that upright individuals and institutions should not deign to be associated with the company, even in the attenuated relationship of stockholder.[341] The symbolic cutting of ties is analogous to the termination of diplomatic relations with a rogue state and the rhetoric is strikingly similar.[342] Beyond depriving the target of any benefit that may be had from maintaining a relationship, it signals that the target of disassociation is such

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336. King & Soule, *supra* note 31, at 438.
337. SOULE, *supra* note 4, at 100.
338. King & Soule, *supra* note 31, at 417.
339. *Id.* at 416–17.
340. *Id.* at 435.
341. *See supra* note 61.
342. *See, e.g.*, Bill McKibben, *Global Warming's Terrifying New Math*, ROLLING STONE, July 19, 2012 (stating the case for divestment from the fossil-fuel industry: "Given this hard math, we need to view the fossil-fuel industry in a new light. It has become a rogue industry, reckless like no other force on Earth. It is Public Enemy Number One to the survival of our planetary civilization.").

a pariah[343] that the actor is willing to forego any benefit that may be had from ongoing contact in order to avoid the taint of being associated with the target.[344] The public and the media would likely find it notable that an investor, especially an institutional investor with a larger stake, would be willing to forego financial rewards in order to make a point. An individual investor who sells a small stake (perhaps held for speculation) in an underperforming company would be less notable than a large, well-known pension fund selling a large stake in a company with strong financial performance. It would have the same expressive effect as the announcement of a large donation, made more notable by the status of the investor as a profit-seeker rather than a do-gooder. In other words, the disassociation message is notable only insofar as it costs the divestor financially. Thus the public relations impact would be directly related to the costs of divestment. As shown above, the actual costs of divesting are minimal.[345] Therefore, an institutional investor who divests in response to constituent pressure could be seen as simply capitulating to avoid the inconvenience of managing unruly activists, at no cost to its portfolio.

While disassociation communicates a meaningful distinction between the divesting investor and the amoral investor who maintains ownership despite the company's bad acts, the impact of disassociation would be significantly reduced in comparison to an investor who maintains her stake in order to agitate for change from within. The activist shareholder is bearing costs to engage with the company,[346] which could also be viewed as a donation to the cause. Where the activist investor announces that she is maintaining ownership solely because she believes she can more effectively agitate for change as a dissident shareholder, the divestor and the activist agree on goals and merely disagree on methods. Thus, to the

343. U.S. CAMPAIGN TO END THE ISRAELI OCCUPATION, DIVEST NOW! A HANDBOOK FOR STUDENT DIVESTMENT CAMPAIGNS 14 (2010), http://www.endtheoccupation.org/downloads/divestguide.pdf ("The goal of a blanket [boycott and divestment campaign] is to pressure Israel to end its military occupation and apartheid policies toward Palestinians by severing all economic relationships with Israel, making it an international pariah."); Small, *supra* note 1, at 2 ("Divestment activists aren't trying to bankrupt Big Oil and Big Coal financially. They're trying to bankrupt them morally—to isolate them as outlaws, just as anti-smoking activists stigmatized Big Tobacco.").

344. *See, e.g.*, DEMOCRACY NOW!, *supra* note 174 (explaining that among the motivations for divestment, investors "have to make a pariah out of these companies. We have to send a message.").

345. *Supra* Part IV.A.1.

346. *See supra* Part IV.A.2.

extent that divestment sends a qualitatively different message than engagement by virtue of disassociation, it is largely a symbolic act of opprobrium.

To say that the act of disassociation is symbolic is not to say that it is meaningless or without value. Symbolism can be a powerful tool for persuasion, beyond rhetoric and reason alone.[347] Symbolic acts of self-sacrifice demonstrate the conviction of the actor more effectively than rhetoric alone and can incite broader change.[348] Citizen movements have employed symbolic acts of condemnation with great success throughout history, from the Boston Tea Party[349] to Occupy Wall Street.[350]

While shareholder engagement offers the advantages of nuanced dialogue, divestment offers the clarity of a simple act. By abandoning an investment in a company, an investor can powerfully state that the company is a pariah—that it is so resistant to positive change, the only option is to cleanse one's portfolio of them.

2. Activists Have More Means of Communication

It is likely that the activist shareholder's expression of disapproval will be heard more loudly by company leadership than the acts of the divestor. The first factor in favor of this conclusion is the means of communication available under each tactic. The divestor's only mode of communication is her sell order: the "Wall Street Walk." While this may be a powerful message, selling shares fore-

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347. *See* Linda L. Berger, *The Lady, or the Tiger? A Field Guide to Metaphor and Narrative*, 50 WASHBURN L.J. 275, 278–80 (2011). Berger discusses the power of conceptual metaphor in the context of persuasive legal writing, noting the importance of metaphor to reasoning and cognition. *Id.* This discussion is applicable here, as metaphor is a type of symbolism.

348. Notable examples of self-sacrificial symbolic acts include Rosa Parks' refusal to give up her bus seat and her subsequent arrest, which catalyzed the Montgomery Bus Boycott, and the self-immolation of Mohamed Bouazizi, which catalyzed the Tunisian revolution and arguably the Arab Spring of 2010–2012. *See Rosa Parks*, WIKIPEDIA, https://en.wikipedia.org/wiki/Rosa_Parks (last visited Apr. 17, 2016) (Rosa Parks); Robert F. Worth, *How a Single Match Can Ignite a Revolution*, N.Y. TIMES, Jan. 21, 2011, http://www.nytimes.com/2011/01/23/weekinreview/23worth.html (Mohamed Bouazizi).

349. *See* DONALD A. GRINDE, JR. & BRUCE E. JOHANSEN, EXEMPLAR OF LIBERTY: NATIVE AMERICA AND THE EVOLUTION OF DEMOCRACY 7111–40 (1991) (discussing the symbolic use of Native American costumes and destruction of tea in the American Revolution).

350. John L. Hammond, *The Significance of Space in Occupy Wall Street*, 5 INTERFACE 499, 502–05 (2013) (discussing the symbolism of locating the protest movement at Wall Street).

closes the avenues of communication available to the shareholder. Of course, the divestor will maintain the ability to engage in outsider tactics, but outsider tactics are available to the activist shareholder as well, so that does not provide a meaningful distinction between the two tactics.

The activist shareholder retains the ability to attend annual meetings. There, she is able to ask pointed questions of company leadership in front of other shareholders. The annual meeting is also an opportunity to meet other shareholders. The activist has the benefit of the shareholder resolution, which the company leadership must review and respond to with either acceptance or rejection. If the proposal makes it onto the proxy, then other shareholders will see the activist's message. Activist investors can also use the implied threat of filing a shareholder proposal as a negotiating tool in order to get concessions from management.[351] The annual meeting and the shareholder proposal are direct, highly visible, high credibility modes of communicating with company leadership.[352] They are also potent means to connect with other shareholders and attempt to enlist their support.[353]

The proxy vote itself is also a potent means of sending a message. Votes in director elections send a clear message of approval or opposition. A shareholder activist can use her vote on resolutions and other matters to steer a company towards a course of reform.

Both the divestor and the engaged shareholder retain the ability to communicate with leadership informally, by letters, e-mails, and phone calls. It is more likely that leadership will take the current shareholder's messages more seriously.[354] This is especially true for institutional investors with large holdings.[355] In recent years, collaborations between corporations and the activists who criticize them have increased.[356] Meaningful informal dialogue increases the chances that concessions will be made.[357]

As a last resort, the activist shareholder may sue the board and company management as a shareholder in a derivative suit.[358] Shareholder derivative suits are rarely used by social activists, likely

351. GOLDSTEIN, *supra* note 150, at 38–39.

352. *See infra* Part IV.C.3.

353. *See id.*

354. *See id.*

355. *See* Sulkowski & Greenfield, *supra* note 109, at 938; Carleton et al., *supra* note 151.

356. Brownstein & Kirman, *supra* note 125, at 73–74.

357. *See id.*

358. *See* Sulkowski & Greenfield, *supra* note 109, at 952–55.

because they are costly[359] and limited to causes of action for breaches of fiduciary duties.[360] However, use of this tactic is not unheard of. For example, shareholders have challenged political contributions made by corporations on the grounds that they constituted waste or *ultra vires* acts.[361] As notable as a large investor divesting ownership of a company may be, it is likely that a subpoena will grab management's attention more effectively. Shareholder litigation is potentially impactful as an activist tool,[362] but it is rarely used.

3. Shareholder Activists Have More Credibility than Divestors

Beyond additional modes of communication, activist shareholders may also enjoy greater weight placed on their messaging than that of a divestor. One factor that can lend greater weight to an activist message when acting as a shareholder is the concept of shareholder primacy. Shareholder primacy is the traditional corporate law concept that a corporation's primary purpose is to act in the best interests of shareholders.[363] In its strongest form, this concept posits that corporate leaders' sole responsibility is to maximize value for the owners of the company—the shareholder value maximization norm.[364] In recent decades, this conception has given way as a binding legal principle to the stakeholder theory, which posits that a corporation should act to further the interests of all constituencies of the corporate enterprise, including customers, employees, and the community.[365] Under the stakeholder theory, a corporation may deviate from optimal profit-maximizing behavior in order to operate in a more socially or environmentally optimal man-

359. In addition to legal fees and court costs, many jurisdictions provide that defendants can demand the plaintiffs post security to cover the defendants' legal costs, to be paid if the suit is unsuccessful. *See* Joseph M. McLaughlin, *Shareholder Derivative Litigation*, Practical Law Practice Note 8-508-8277, at 36 (2016), Westlaw.

360. *Id.* at 3.

361. *See* William Alan Nelson II, *Post-*Citizens United*: Using Shareholder Derivative Claims of Corporate Waste To Challenge Corporate Independent Political Expenditures*, 13 Nev. L. J. 134, 151–55 (2012).

362. *See* Sulkowski & Greenfield, *supra* note 109, at 945–54 (discussing litigation based on the *ultra vires* doctrine as a potential means for pressuring corporations to change policy).

363. Lisa M. Fairfax, *The Rhetoric of Corporate Law: The Impact of Stakeholder Rhetoric on Corporate Norms*, 31 J. Corp. L. 675, 676–77 (2006).

364. *See* Stephen Bainbridge, *A Duty to Shareholder Value*, N.Y. Times (Apr. 16, 2015, 6:46 AM), http://www.nytimes.com/roomfordebate/2015/04/16/what-are-corporations-obligations-to-shareholders/a-duty-to-shareholder-value.

365. Fairfax, *supra* note 363.

ner.[366] Corporate law now embraces a broader mandate for corporate leaders to take into account the interests of groups other than shareholders.[367]

Despite the evolution of the law on this point, evidence shows that shareholder primacy and value maximization remain strong social norms guiding corporate managers.[368] This is an understandable result of incentive-based compensation tied to share price, business school curriculum that focuses on value maximization, and the structure of corporate governance itself.[369] Since shareholders elect the directors, who in turn hire the CEO, company leaders are ultimately accountable to shareholders for their performance even if they would avoid legal liability for their business decisions.[370] The shareholder primacy norm is reinforced by laws that require annual shareholder meetings and shareholder approval of certain actions and regulations that mandate extensive proxy disclosures and allow shareholders to propose resolutions.[371] Thus, a company's leadership is more likely to be responsive and deferential to an activist lobbying for change as a shareholder. Once an activist divests her shares, she no longer enjoys the privileged status of shareholder in the eyes of management and becomes a mere secondary stakeholder—a member of the community.

Awareness of the broader stakeholder conception of the corporate purpose has increased in recent years.[372] Business leaders' perception of the importance of corporate social responsibility has

366. N. Craig Smith & David Ronnegard, *Shareholder Primacy, Corporate Social Responsibility, and the Role of Business Schools*, 26–27 (INSEAD, Faculty & Research Working Paper No. 2014/13/ATL/ISIC, 2014), http://ssrn.com/abstract=2322780.

367. Fairfax, *supra* note 363.

368. Smith & Ronnegard, *supra* note 366, at 13–14.

369. *Id.*

370. *Id.* at 16.

371. GARNER & GEISSINGER, *supra* note 142, at 8–9, 13–39, 50. Notably, another SEC regulation requires public companies to disclose in their proxy statement their process for shareholders to communicate with the board of directors, or if they don't have such a process then they must disclose the basis for their view that such a process is inappropriate. 17 C.F.R. § 229.407(f).

372. Fairfax, *supra* note 363, at 690–97. *See also* THE CONFERENCE BOARD GOVERNANCE CENTER, *supra* note 152, at 8 ("While the ultimate goal of a public corporation is to maximize shareholder value, it can only do so on a sustainable basis by serving all its constituents. An optimally balanced system of corporate governance is based on the premise that serving the interests of major constituencies of corporations-customers, employees, creditors, suppliers, communities, and the environment-is essential to maximizing shareholder value.").

increased as well.[373] According to a 2015 survey of international business leaders by Accenture, "93% of CEOs surveyed believe that environmental, social and governance issues will be 'important' or 'very important' to the future success of their business."[374] However, company leadership's impulse to do good creates tension with their responsibility to control costs and maximize profits. It is likely that the corporate world's embrace of corporate social responsibility is based on a better understanding of the reputational harms of irresponsible behavior[375] and the profitability gains offered by investing in communities,[376] rather than some moral evolution. If that assumption is correct, management would still reject a reform that ultimately hurts the bottom-line—they would just consider more factors before rejecting it.

However, the tension between shareholder and stakeholder interest is alleviated when a shareholder activist is lobbying for the reform. The shareholder wealth maximization norm is based on the (perhaps outmoded) notion that the corporation is the property of the shareholder, the manager is acting as a trustee of that property, and therefore the corporation should only be used for the benefit of the owner.[377] In the context of shareholder proposals, even though the proposals are precatory, management should seriously consider shareholder proposals that garner substantial support.[378] When the owner signals her support for a socially beneficial reform, management should not feel conflicted even if the reform is not justified in terms of cost. Where a shareholder resolution is supported by 100% of the shareholders, the mandate to enact the reform would be clear, regardless of the costs. On the other hand, where a resolution only achieves 1% support and clearly goes against the economic interests of the other 99%, the mandate to reject would be almost as stark. For cases in between, management

373. *Valuing Corporate Social Responsibility: McKinsey Global Survey Results*, McKinsey & Company (Feb. 2009), http://www.mckinsey.com/insights/business-functions/strategy-and-corporate-finance/our-insights/valuing-corporate-social-responsibility-mckinsey-global-survey-results.

374. Accenture, *supra* note 20, at 17.

375. *See, e.g.*, Sheila Bonini, David Court, & Alberto Marchi, *Rebuilding Corporate Reputations*, McKinsey Quarterly (June 2009), http://www.mckinsey.com/global-themes/leadership/rebuilding-corporate-reputations.

376. *See, e.g.*, Howard Schultz, *Invest in Communities To Advance Capitalism*, Harv. Bus. Rev. (Oct. 17, 2011), https://hbr.org/2011/10/ceos-should-invest-in-communit.

377. Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 Wash. & Lee L. Rev. 1423, 1427–28 (1993).

378. Business Roundtable, 2012 Principles of Corporate Governance 31 (2012).

should feel incrementally more comfortable pursuing a socially responsible policy that may impose bottom-line costs in proportion to the amount of support among shareholders. So at least in theory, activist shareholders should face less resistance and wield greater persuasive power than outsiders lobbying for change.

Another factor that increases the persuasive power of an activist shareholder's message, vis-à-vis divestors or outsiders, is her ability to employ business-related justifications for her proposed reforms.[379] Intuitively, it is understandable that management would be more receptive to reforms that are justified in terms of value maximization or which include business justifications along with social value justifications. Business leaders tend to think in narrow terms of increasing revenues, decreasing costs,[380] and maximizing shareholder value.[381] If the costs of implementing a reform can be justified in financial terms, then there will not be any tension between the shareholder value maximization norm and concern for the broader community.[382] Just as importantly, management will not be risking the value of their incentive-based compensation or their reputations as savvy businesspersons.

As an illustration, shareholder activists targeting Coca-Cola have been particularly effective at employing business-based frames in their discussion of reform. In connection with the successful effort to focus Coca-Cola's attentions on the threats posed by HIV/AIDS in the developing world,[383] one shareholder activist pointed out the business risks posed by the disease, "thereby tinging their proposal with Christian concern and economic rationality."[384] Another activist used Coke's own marketing slogans to frame their demands,[385] implying that the company was acting inconsistently. In another effort focused on Coca-Cola's complicity in violence against labor unions in Colombia, an assistant comptroller for union pension policy stated that "when there is 'mistrust' and 'sus-

379. Goldstein, *supra* note 150, at 41 ("[A]n asset manager who also frequently engages on [environmental and social] topics felt that companies are more willing to act if 'a business case is being made[.]'").

380. Michael E. Porter & Mark R. Kramer, *Creating Shared Value: Redefining Capitalism and the Role of the Corporation in Society*, 89 HARVARD BUS. REV. 62, 65–67 (2011).

381. Smith & Ronnegard, *supra* note 366, at 19–24.

382. *See generally* Porter & Kramer, *supra* note 380; Michael E. Porter & Mark R. Kramer, *The Link Between Competitive Advantage and Corporate Social Responsibility*, 84 HARVARD BUS. REV. 78 (2006).

383. *See supra* Part IV.A.3.

384. Foster, *supra* note 231, at 196.

385. *Id.* at 188.

picion' of a company, its shareholders are at financial risk."[386] The board opposed the activist's resolution, but committed to a review of the company's human rights policies in collaboration with investors and made a ten million dollar donation to support victims of violence in Colombia.[387]

The effectiveness of employing economic justifications for changes in corporate policy also finds some support in empirical observation. For example, a 2010 McKinsey survey asked business executives which reasons would be most likely to compel them to "take a women-specific focus in developing and emerging economies."[388] The financial motivations of "[a]dditional value to be generated by investing in women specifically" and "[i]mprovement of company performance" were selected by 25% and 10% of respondents, respectively.[389] The external motivations of "[s]tated need of one or more local communities in which we operate," "[g]lobal giving trends," and "[r]esponse to media/[NGO] pressure" were selected by 15%, 4%, and 3% respectively.[390] Indeed, an earlier survey found that 90% of executives were "motivated to champion social or environmental causes by profitability or improving public relations."[391] The Accenture study found a consensus among business leaders that sustainability efforts "must lead to business value."[392]

One would expect other shareholders to also be more receptive to socially beneficial reforms when supported by business justifications. Shareholders face a similar tension to that faced by management: where a particular reform stands to provide social benefits but is not justified financially, they must choose between the returns on their investment and doing the right thing. However, where a given reform stands to increase, or at least not decrease, the value of their investment then the conflict is resolved. Thus, we would expect other shareholders to support changes that are justified, at least in part, by business reasons at a higher rate than changes motivated solely by ethical or sustainability rationales.

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386. *Id.* at 201.

387. *Id.* at 202.

388. McKinsey & Co., *Rethinking How Companies Address Social Issues: McKinsey Global Survey Results*, McKinsey Insights (Jan. 2010), http://www.mckinsey.com/insights/winning_in_emerging_markets/rethinking_how_companies_address_social_issues_mckinsey_global_survey_results.

389. *Id.*

390. *Id.*

391. Smith & Ronnegard, *supra* note 366, at 15.

392. Accenture, *supra* note 20, at 36.

This intuition is supported by empirical evidence that shows shareholders are more likely to support shareholder resolutions that emphasize value-maximization rather than parochial concerns.[393] Such frames are more likely to draw support from large institutional investors, who may be agnostic about social or environmental issues, where the proposals may improve the value of a company.[394] Greater support among shareholders would, in turn, serve to further ease the tension faced by business leaders between pursuing the greater good and the shareholder wealth maximization norm.[395]

Activist shareholders, compared to outsiders, will enjoy greater credibility when framing the justifications for reform in financial terms. The experience of ExxonMobil provides a recent illustration of this phenomenon. As You Sow, a non-profit environmental advocacy group, partnered with wealth management firm Arjuna Capital to submit a shareholder resolution[396] seeking a report on ExxonMobil's "strategy to address the risk of stranded assets presented by global climate change, including analysis of long and short term financial and operational risks to the company."[397] In response, ExxonMobil agreed to publish its first carbon asset risk assessment if the activists withdrew their shareholder resolution.[398] Arjuna Capital's director of equity research and shareholder engagement responded by saying:

> Shareholder value is at stake if companies are not prepared for a low-carbon scenario. More and more unconventional 'frontier' assets are being booked on the balance sheet, such as deep-water and tar sands. These reserves are not only the most

393. *See* Schwab & Thomas, *supra* note 41, at 1035–36 ("Still, to be successful, union-shareholder activism must gain the support of other shareholders. This is most likely to occur when unions embrace a goal of maximizing firm value–clearly a new way of thinking for some unions. Other shareholders are naturally suspicious of unions' motives, and union-shareholder activism will remain quixotic unless the proposals plainly attempt to maximize overall firm value, rather than promote narrow union interests.").

394. *See* Landier & Nair, *supra* note 11, at 39.

395. *See supra* Part IV.C.3.

396. Press Release, As You Sow, Landmark Agreement with Shareholders: ExxonMobil Agrees To Report on Climate Change & Carbon Asset Risk (Mar. 20, 2014), http://www.prnewswire.com/news-releases/landmark-agreement-with-shareholders-exxonmobil-agrees-to-report-on-climate-change—carbon-asset-risk-251219111.html.

397. As You Sow, 2014 Exxon Mobil Shareholder Resolution (2014), http://www.asyousow.org/wp-content/uploads/2014/03/exxonmobil2014carbonbubble.pdf.

398. Press Release, As You Sow, *supra* note 396.

> carbon intensive, risky, and expensive to extract, but the most vulnerable to devaluation. As investors, we want to ensure our Companies' capital will yield strong returns, and we are not throwing good money after bad.[399]

Since the value of activist shareholders' investment depends on the ongoing performance of the company, they have "skin in the game," so to speak.

On the other hand, divestors and other outsiders do not have a financial stake in the company, so they are more likely to be perceived as acting cynically when framing their grievance in economic terms and thus given less weight. This intuition is given empirical support by a study conducted by Ion Bogdan Vasi and Breydon G. King.[400] This study analyzed the perceived environmental risk of the largest 700 companies in the United States, as measured by environmental risk ratings from a provider of extra-financial research over a five-year period.[401] They found that insider tactics, namely shareholder resolutions on environmental issues, had a negative effect on the companies' environmental risk perceptions while outsider tactics, namely boycotts, protests, and lawsuits, did not produce a significant effect.[402] Vasi and King speculate that "[b]ecause risk analysts perceive that shareholder activists' interests are more closely aligned with those of the firm, shareholder engagement sends a clearer signal to investors about the potential liabilities of unsound environmental practices."[403] They also found that environmental risk negatively affects a company's financial performance; even though shareholder resolutions focused on the environment were not shown to directly impact financial

399. *Id.*

400. Ion Bogdan Vasi & Breydon G. King, *Social Movements, Risk Perceptions, and Economic Outcomes: The Effect of Primary and Secondary Stakeholder Activism on Firms' Perceived Environmental Risk and Financial Performance*, 77(4) AMERICAN SOCIOLOGICAL REVIEW 573 (2012). Vasi and King suggest that outsider tactics are more effective at actually changing corporate behavior than insider tactics. *Id.* at 589. However, Eesley and Lenox suggest it is the outsiders' confrontational tactics, not the group's legitimacy, that are driving this difference. *Supra* note 241, at 777. This observation does not defeat the point here: activists pursuing an engagement strategy may also pursue outsider tactics. In other words, exercising voice as an insider does not foreclose the possibility of exercising voice as an outsider. Indeed, the exercise of shareholder voice should be considered a reinforcement of messages from external influences on management, not an isolated act. SIMON ET AL., *supra* note 68, at 51.

401. Vasi & King, *supra* note 400,. at 579.

402. *Id.* at 586.

403. *Id.* at 588.

performance, they may indirectly hurt financial performance through increased perception of risk.[404]

Another shared value that shareholder activists will be well-positioned to emphasize is concern for a company's reputation. Executives regard improving reputation as the primary business goal of investing in CSR efforts.[405] Shareholders are literally invested in the company's wellbeing and future prospects, which signals a degree of commitment and, since the value of their investment is yoked to the fate of the company, communicates that they belong to the same community of interest as the company leadership and the other shareholders. They would naturally be concerned about the company's reputation. Divestors, on the other hand, have made the choice to disassociate themselves from the company. Therefore, any appeal that they may make based on the reputation of the company would rightly be perceived as a cynical appeal to management's sensitivities, rather than a natural concern based on shared values.

This insight is illustrated by the experience of Talisman Energy, a Canadian oil and gas company that owned an interest in an oil operation in Sudan. Talisman became the focus of an intense shareholder campaign to disinvest from Sudan that included shareholder resolutions, contentious annual meetings, and divestment by large institutional investors.[406] Advocates not only made moral arguments for disinvestment but also pointed to financial risks: sanctions and litigation, reputational harms, and the uncertainty of operating in the war-torn country.[407] In 2002, Talisman decided to sell its interest. In explaining the decision, Talisman's CEO said, "Talisman's shares have continued to be discounted based on perceived political risk in-country and in North America to a degree that was unacceptable for 12% of our production. Shareholders

404. *Id.* at 586–88.

405. *Tackling Sociopolitical Issues in Hard Times: McKinsey Global Survey Results*, MCKINSEY & CO. (Nov. 2009), http://www.mckinsey.com/insights/corporate_social_responsibility/tackling_sociopolitical_issues_in_hard_times_mckinsey_global_survey_results.

406. HUMAN RIGHTS WATCH, SUDAN, OIL, AND HUMAN RIGHTS, 416–37 (2003), https://www.hrw.org/sites/default/files/reports/sudanprint.pdf.

407. Eric Reeves, *Talisman Energy Share Price Continues To Suffer*, SUDAN RESEARCH, ANALYSIS, AND ADVOCACY (Nov. 9, 2001), http://sudanreeves.org/2004/12/22/talisman-energy-share-price-continues-to-suffer-november-19-2001 (pointing out concerns over legal liability and reputational harm); Eric Reeves, *Talisman Energy's Vulnerability to a Divestment Campaign*, SUDAN RESEARCH, ANALYSIS, AND ADVOCACY (March 2, 2000), http://sudanreeves.org/2004/12/13/talisman-energys-vulnerability-to-a-divestment-campaign-march-2-2000/ (noting the likelihood of sanctions against Talisman).

have told me they were tired of continually having to monitor and analyze events relating to Sudan."[408] Since Talisman was facing litigation, sanctions, and a divestment campaign, their change of heart cannot be attributed solely to engagement efforts, but the rhetoric surrounding their withdrawal suggests that the company leadership was influenced by arguments based around shared concerns such as share price and risk.

When shareholder activists frame their grievances in terms of profitability, risk, or reputation, it will be more difficult for companies to dismiss their concerns. Generally, "[i]nvestors are viewed as more moderate in their views and relatively mainstream compared to radical or liberal groups that target corporations."[409] For outsiders hearing these messages it may be impossible to distinguish between shareholders motivated by ethics and those motivated purely by value maximization. For example, when activist investors in Dow wrote a letter to the SEC expressing the view that Dow had failed to account for the risks related to the gas leak tragedy in Bhopal, India, a newspaper reported the letter was sent by "shareholders" and "investors," not activists.[410] In fact, in the case of institutional shareholders that represent diverse constituencies, like university endowments and public employee pension funds, it may be impossible even amongst themselves to disaggregate the profit motive from social motives. The perception of shareholders as more mainstream and the difficulty of discerning their precise motivations make it more difficult for management to dismiss shareholders' concerns compared to a radical, marginal group's narrow social agenda.

The activist's use of a "shared values" frame will be seen as having higher credibility than a divestor. The divesting activist, as an outsider without a financial stake in the company, will be perceived as acting cynically when framing her grievance in economic terms. The divesting activist will be confined to employing appeals to ethics and sustainability, rather than shared values.

4. Exit Forecloses Voice

When a shareholder decides to sell her shares in protest, the opportunity to use the tools of shareholder engagement is fore-

408. Press Release, Talisman Energy, Talisman to Sell Sudan Assets For C$1.2 Billion (Oct. 30, 2002), http://www.prnewswire.com/news-releases/talisman-to-sell-sudan-assets-for-c12-billion-76560867.html.

409. LANDIER & NAIR, *supra* note 11, at 48–49.

410. Manjeet Kripalani, *Poisonous Legacy: Is Dow Chemical Liable for Bhopal?*, SPIEGEL ONLINE (May 29, 2008, 11:07 AM), http://www.spiegel.de/international/business/poisonous-legacy-is-dow-chemical-liable-for-bhopal-a-556243.html.

closed and only outsider tactics are left. By rendering herself an outsider, her ability to affect corporate policy through engagement is reduced.[411] While activists may be able to persuade company leadership that divestment is prudent due to financial risks, such arguments coming from outsiders are unlikely to make company leadership second-guess their own cost-benefit analyses. This is likely to be the case unless investors depart in sufficient numbers to depress stock price, which is extremely unlikely.[412]

Those who divest will lose access to shareholder meetings. They may be able to reach out to shareholders by staging protests outside the meeting, communicating their message via signs and leaflets. Activist shareholders on the other hand will be able to attend the meeting and participate in the Q&A sessions inside the meeting. This may focus the attention of shareholders on the activist shareholder's message more acutely. The other shareholders may be more willing to listen to the activist shareholder's message, since they may attach more weight to communications that come through the formal channels available to shareholders.

On the other side, if an activist shareholder maintains her shares, she may avail herself of engagement tactics without foregoing the option of divestment. To the extent that divestment is seen as a threat to the corporation, activist shareholders can use the threat of divestment as an effective means to influence company leadership to bolster their efforts at persuasion.[413] Engagement provides a mechanism to formally notify the company of its objectionable behavior, propose changes, and, if these efforts are unsuccessful, divest the shares.

As an illustration, Norway's Government Pension Fund has a nuanced approach to shareholder engagement.[414] As a first step, the fund votes its shares according to responsible investment guidelines.[415] Next, the committee reviews portfolio companies for compliance with the fund's ethical and sustainability criteria.[416] When a company is flagged for non-compliance, the fund sends the company notification and provides an opportunity for response.[417] Fi-

411. *See supra* Part IV.C.3.

412. *See supra* Part IV.B.1.

413. Admati & Pfleiderer, *supra* note 51, at 2673–76. Note that Amati and Pfleiderer's conclusion is confined to the case where the activist holds a sufficiently large stake such that share price would be depressed if she sold.

414. *See* Chesterman, *supra* note 61, at 582–91.

415. *Id.* at 588.

416. *Id.* at 588–91.

417. *Id.* at 590–91.

nally, the fund will divest if they don't receive a satisfactory response.[418] Taking this approach, an investor can have a positive impact through the ballot box, have a meaningful engagement with the company over issues, and then, upon exit, send a powerful message.

An "engage then divest" strategy may prove more effective than simply divesting, since the activist will be able to assert that she attempted to reform the company, but the company was unwilling or unable to reform. Such an assertion would lend credibility to attempts to cast the company as a pariah or bad corporate citizen. The availability of this higher-credibility assertion post-exit may increase the leverage that the activist would enjoy pre-exit: the threat of exit and shaming may make management more willing to engage with the activist. In Hirschman's words, "[o]nce you have exited, you have lost the opportunity to use voice, but not vice versa"[419] and "the effectiveness of the voice mechanism is strengthened by the possibility of exit."[420]

D. Engagement as Information-Forcing Mechanism

Beyond additional means of messaging and employing higher quality frames, activist shareholders are also able to force disclosure by the company in ways that divestors are not. They have the "soft power" to engage with leadership informally and request information through dialogue. They also have the ability to propose shareholder resolutions requiring the corporation to investigate and disclose the scope of their activities and the impact of those activities.[421] For example, in response to *Citizens United*, there has been a dramatic increase in the number of shareholder proposals urging companies to disclose their political spending, some of which have achieved some degree of success.[422] Shareholders also retain the "hard power" to examine the corporation's books and records under Delaware law.[423]

418. *Id.* at 591–94.

419. HIRSCHMAN, *supra* note 47, at 37.

420. *Id.* at 83 (emphasis removed).

421. *See, e.g.*, OFFICE OF THE NEW YORK CITY COMPTROLLER, *supra* note 136, at 3 ("AIG, Bank of NY Mellon and U.S. Bancorp agreed to disclose the breakdown of their workforce by race and gender for major job categories, including senior management.").

422. Sach, *supra* note 14, at 941–42; *see also* GOLDSTEIN, *supra* note 150, at 35–36.

423. *See* DEL. CODE ANN. tit. 8, § 220 (2016). A shareholder's power to inspect the books and records of a company is limited to purposes "reasonably related to such person's interest as a stockholder." *Id.* The activist may be able to satisfy this

The information obtained through these means can be used to educate investors about the commercial risks that a certain practice poses for a company.[424] For example, the UK's Carbon Disclosure Project recruits institutional investors to persuade companies to disclose information regarding their environmental externalities.[425] The group then analyzes the data and utilizes shareholder pressure to encourage companies to reform.[426]

Where the disclosed practice represents offensive conduct or a departure from the company's image, the information can be disclosed to the media or other investors to inflict reputational harm. The information can also be used by the activists to identify other issues and to inform the activist's campaign efforts, both as insiders interacting with the corporation and as outsiders pushing for reform on other fronts. For example, the Laborers International Union of North America (LiUNA) targeted large homebuilders for their role in the 2008 mortgage crisis with an array of outsider tactics, including public protests and congressional contact efforts.[427] They also proposed shareholder resolutions at banks in which their pension fund held shares, which would have required disclosure of the types of mortgages that the banks bought and sold.[428] The stated purpose of the requested disclosure was to allow investors to better evaluate risk, which alone would raise concerns among the company leadership and other shareholders.[429] But the disclosure may have provided LiUNA with additional information that would make fodder for the other elements of their mortgage campaign.

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requirement by framing their demand in terms of a business-related justification, such as waste and mismanagement. *See also* William Allen Nelson II, *Post-*Citizens United*: Using Shareholder Derivative Claims of Corporate Waste To Challenge Corporate Independent Political Expenditures*, 13 NEV. L. J. 134, 149–52 (2012).

424. *See* Jonathan G. Koomey, *This Is a Huge Deal: Exxon Agrees To Evaluate the "Stranded Asset" Risk Associated with Climate Action*, JONATHAN KOMOMEY: BLOG (Mar. 21, 2014), http://www.koomey.com/post/80325189354 (discussing ExxonMobil's Carbon Asset Risk report: "So the pressure will continue to build, and soon the disclosures will result in attention paid to this asset risk that simply hasn't been present before. That attention will become a flood very rapidly. It's the beginning of the end of the fossil fuel economy, but the big players just don't realize it yet (or if they realize it, they're not admitting it).").

425. *About Us – CDP*, CARBON DISCLOSURE PROJECT, https://www.cdp.net/en/info/about-us (last visited Sept. 28, 2016).

426. *Id.*

427. SOULE, *supra* note 4, at 140–41.

428. *Id.* at 141.

429. *Id.* at 141.

E. Exit Leaves Corporations Unconstrained

Activists must also consider the change in shareholder constituency that a successful divestment campaign will cause. If a divestment campaign were successful in persuading all socially conscious investors to sell their shares and dissuading socially conscious investors from buying shares, the company's shareholder body would be effectively cleansed of conscience. In this case, the fiduciary responsibilities of the company management become quite clear: they would owe no duty to the shareholders to consider the issue that was the subject of the divestment campaign.

Hirschman refers to a similar paradox in the context of schools, wherein quality-conscious parents may exit poorly performing public schools in favor of private schools. The result leaves public schools with a constituency much less likely to exercise the political mechanism of voice, and thus less likely to achieve reform than before the exit option was exercised.[430] Thus, exit can have a "corroding influence" on the "vigorous and constructive" exercise of voice.[431]

In a more likely scenario, where some number of conscientious investors divest, the change would still have the effect of moving a percentage of ownership out of the hands of those who value social or environmental responsibility to those who do not, or at least those who are agnostic. Management in this scenario would feel less concern for facing objections from shareholders at shareholder meetings and through shareholder resolutions. The divesting activist's appeals to the shareholder constituency in the future will be hampered by the activists' inability to attend the special meeting, propose shareholder resolutions, and employ shared values frames with credibility. Corporate leadership may still worry about the opinion of other stakeholders and the general public, but in relation to the constituency that matters the most, the shareholders, the result of divestment will be to decrease or eliminate pressure, not ratchet it up.

F. Divestment Is Superior when Reform Is Impossible

Finally, it is worth noting one circumstance where divestment would seem to be a clearly better alternative: when the desired change in policy would represent an existential threat to the company. Where the core business of the company is itself the problematic behavior, capitulating to an activist demand would effectively

430. HIRSCHMAN, *supra* note 47, at 45–46.
431. *See id.*, at 61.

require the company to cease operations. One notable example was a shareholder resolution put forward in 1990 by religious groups holding stock in Philip Morris.[432] Their resolution would have required the company to "cease tobacco operations."[433] A more current example is found in the Fossil Free campaign's demands that the top 200 companies holding fossil fuel reserves immediately stop exploring for new hydrocarbons, stop lobbying lawmakers to preserve their special treatment, and pledge to "keep 80% of their current reserves underground."[434] Divestment proponents acknowledge that fossil fuel companies will not comply with their demand, nor will they be able to get shareholders to support them.[435] As one divestment proponent put it, Fossil Free's demands are reasonable given the exigencies of climate change, but "[g]iven the norms of corporate capitalism, these are audacious, even preposterous demands."[436]

Complying with these demands would almost certainly render these companies unprofitable and send them into bankruptcy. The costs of making these changes would dwarf any costs imposed by divestment or shareholder engagement so it would never be rational for management to accede to the activists' demands. In such cases, the traditional methods of engagement would be unlikely to elicit a response: management would refuse to take steps which would render the company insolvent and other shareholders would refuse to support measures that would obliterate the value of their investment. As a 350.org supporter said, "the problem with the fossil fuel industry is the product itself. It is not plausible that [University of Toronto] could attend a shareholder meeting of Peabody Energy and convince them to stop digging up and burning coal."[437] Engagement simply is not an option where the very nature of a company's business is problematic.[438]

Divestment is also likely to be futile in changing company behavior in these circumstances.[439] Where both tactics would be ineffective at directly changing corporate behavior, divestment would be the better option for three reasons: (1) divestment would save the investor the definite costs of engagement discussed above; (2)

432. Teoh et al., *supra* note 98, at 35–36.
433. *Id.*
434. *FAQ*, FOSSIL FREE, http://gofossilfree.org/faq/ (last visited Sept. 28, 2016).
435. *Id.*
436. Small, *supra* note 1, at 1.
437. TORONTO 350.ORG, *supra* note 5.
438. Richardson, *supra* note 15, at 136 n.46.
439. LANDIER & NAIR, *supra* note 11, at 71.

divestment would be more effective at casting the company as a pariah, since the exercise of voice in the form of shareholder engagement implies that the company is capable of reform;[440] (3) divestment would provide the symbolic impact benefits of disassociation.[441]

In the words of *The Ethical Investor*, in the face of futility "there is merit in dissolving ties with the corporation in order to prevent being locked in to a policy that is morally repugnant" and doing so may have the symbolic effect of "a last-ditch effort to avert social harm."[442]

V.
CONCLUSION

Engagement generally is superior to divestment as a tactic to change corporate behavior. Both tactics have limited ability to inflict direct costs on the corporation. Theoretically, divestment may be able to drive share prices down, but the chance of achieving the necessary critical mass is unlikely due to the sheer size of the market for corporate equity and the countervailing pressures which would frustrate the effort. Engagement will inflict some direct costs in terms of the time and effort of company leadership in communicating with the shareholder activist and responding to shareholder resolutions. While these costs may be especially salient to the decision makers within the corporation, they are relatively insignificant to a large corporation.

Thus, the more important means for influencing corporate leadership is through the messages that the respective tactics can send. Engagement offers the unique means of communication available to shareholders, allowing activists to reach out to company leadership and other shareholders through formal means. The shareholder primacy norm and high credibility shared values frames suggest that the messages of activist shareholders will be more persuasive to these audiences. Messages from shareholders will also be viewed as more credible by the media, the general pub-

440. *See supra* Part III.A.

441. Activists could consider shifting their focus to encouraging the company to make incremental reforms which would not threaten the company's continued survival. For example, 350.org could encourage fossil fuel companies to improve their extraction methods or to invest more in renewable energy sources. Such a shift in focus would constitute a strategic choice (a question of which corporate behavior to incentivize) not a tactical choice, and thus is beyond the scope of this Note.

442. SIMON ET AL., *supra* note 68, at 26.

lic, and other shareholders, which increases the shareholder activist's ability to inflict reputational harm if friendly negotiations with company leadership are unproductive.

Divestment, on the other hand, only offers a message of disassociation. This message may provide some consolation where the corporation is incapable of reform. But where engagement is a viable alternative, divestment becomes a purely symbolic act of disdain.

A divestment campaign that moves ethical shareholders out of the shareholder body will have the unintended consequence of leaving the corporate leadership less constrained. By divesting, the activist forecloses the opportunity for exercising voice, while the engaged activist retains the option of divesting if her engagement efforts prove futile. If that happens, a subsequent divestment will not just express disdain but suggest that the corporation is unwilling or unable to reform: a true rogue actor. Thus, engagement is a superior tactic to divestment except where the corporation is incapable of reform or where the activist and supporting shareholders lack the resources to press an engagement effort.

Activism targeting corporations is here to stay. Wise activists will seek to enlist allies with a stake in the targeted corporations and use their platform to send a clear message to company leadership as well as outsiders. By illuminating the relative utility of divestment and engagement, hopefully the analysis herein will allow activists to make more informed decisions when contemplating a shareholder-focused anti-corporate campaign. It is the author's hope that it will contribute to a frank discussion about what is at stake.