

Will shareholder voices be silenced under Trump's SEC?

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Donald Trump's nomination of Paul Atkins to SEC chair is likely a harbinger of hushed shareholder voices in the upcoming administration © REUTERS

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Institutional investors and pension funds will need to look to the private enforcement of federal securities laws

At a glance

- Donald Trump's nomination of Paul Atkins to SEC chair is likely a harbinger of hushed shareholder voices in the upcoming administration.
- With Atkins steering the ship, the SEC is expected to dial back enforcement actions and civil penalties imposed on public companies for corporate wrongdoing.
- One way institutional investors can equip themselves for such change is by understanding the influence they can gain by monitoring their portfolio and, when appropriate, threatening and commencing litigation to recover losses and seek corporate change.

Founded in 1934, the Securities and Exchange Commission is the US federal regulatory agency tasked with protecting investors and maintaining fair and efficient markets.

The agency was created after congressional hearings revealed that numerous financial institutions had misled investors, acted irresponsibly and participated in rampant insider trading — all of which contributed to the stock market crash of 1929 that shuttered the doors of some 5,000 banks and left nearly 2mn people homeless.

The agency is led by up to five commissioners and one chair, all of whom are appointed by the president subject to approval from the Senate. The appointment of the chair is particularly important given the ability to set the agency's agenda and priorities.

Since its establishment, the SEC has worked closely with the Department of Justice to prosecute individuals and corporations for violations of federal securities laws, and such work has complemented the actions of private and institutional investors in seeking legal redress against negligent and/or fraudulent corporates, typically via shareholder litigation.

Shareholder litigation is a powerful tool in promoting good corporate behaviour, but it is by no means the only method available to investors.

The SEC promulgates several rules that allow investors to advance corporate reforms, such as the shareholder proposal rule. This allows investors to submit proposals to be included in a company's proxy statement for consideration at their annual meeting.

Since its promulgation, the rule has provided fertile ground for investor voices to flourish and drive corporate change. Civil rights activists holding shares in public companies relied on it in the 1950s to protest against the segregated bus seating policies of the Greyhound bus company.

And at the height of the Vietnam war, a human rights group holding shares in the Dow Chemical Company submitted a proposal that urged the company to cease its production of napalm — the deadly gel that melted flesh, caused carbon monoxide poisoning and cleared out bunkers and trenches.

The shareholder proposal rule also enjoyed substantial use under the Biden administration, due in large part to the efforts of SEC chair Gary Gensler, who issued guidance that made it more difficult for companies to exclude such proposals.

In 2023, shareholders submitted nearly 900 resolutions to be discussed at annual meetings — more than 65 per cent of which concerned questions of social policy, including environmental issues or the promotion of diversity initiatives.

From Gensler to Atkins

However, Donald Trump's nomination of Paul Atkins to SEC chair is likely a harbinger of hushed shareholder voices in the upcoming administration. Not only has Atkins openly criticised the guidance that led to the proliferation of environmental, social, governance and climate-related shareholder proposals under Biden and Gensler, but Trump affiliates predict he is likely to reverse many of the policies pursued under their leadership.

Trump's nominations are not the only indication of what is to come in the early days of his presidency.

With public companies bowing out of environmental initiatives like the Net-Zero Banking Alliance and buckling under political pressure before Trump's inauguration, institutional investors and pension funds should be prepared for change as seismic as it is swift.

With Atkins steering the ship, the SEC is expected to dial back enforcement actions and civil penalties imposed on public companies for corporate wrongdoing.

Atkins, who served as an SEC commissioner before the 2008 financial crisis, once critiqued the imposition of civil penalties against corporations as being unpredictable and "justified on little more than that they 'feel right'". Such sentiment emboldens corporations, is likely to increase their fraudulent behaviour and will result in unrecovered losses for pension funds and institutional investors alike.

One way institutional investors can equip themselves for such change is by understanding the influence they can gain by monitoring their portfolio and, when appropriate, threatening and commencing litigation to recover losses and seek corporate change.

Even with a progressive SEC, institutional investors have realised the importance of shareholder litigation given that shareholder proposals are widely dismissed or ignored — only 5 per cent of shareholder proposals submitted in 2023 passed a vote.

Legal scholars and institutional investors agree that the impact of private enforcement of the federal securities laws is not to be understated.

In a recent case before the Supreme Court, lawyer Brian Fitzpatrick said: "The government is a far inferior substitute for private enforcement of the law — which is exactly why petitioners and their multibillion-dollar corporate amici like it."

Amid the political sea change anticipated under Trump's second administration, it is critical that institutional investors and pension funds retain experienced counsel to monitor their portfolios and understand their options for recovery of any losses and actions to deliver corporate governance reforms.