Revisiting the Proxy Contest

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The poison pill forever changed the hostile deal. It allows a board to “just say no” and forces a hostile bidder to run a proxy contest to remove and replace the board to eliminate the pill impediment. If a target is well-defended and prohibits shareholder action by written consent or the calling of a special meeting, then the proxy contest is confined to the annual meeting.

According to Factset Sharkwatch, the majority of public companies (about 79 percent), bar either the calling of special meetings by shareholders or otherwise prohibit shareholders from acting by written consent. This means the annual meeting is typically the focal point for any hostile bid.

It is now proxy season, so expect hostile activity to increase as bidders time their hostiles to include the potential pressure of a proxy contest. With it we have begun to see a trickle of these contests, including CF Industries’ hostile offer for Terra Industries and Astellas Pharmaceuticals’ hostile offer for CV Therapeutics.

The proxy contest decision would seem to be a no-brainer. A well-planned hostile will pair a proxy contest with an exchange or tender offer. The latter is to table the offeror’s bid while the former is necessary to force the board to deal. Few, if any hostiles for a full slate of the board actually reach an election.

If the target is going to lose, they capitulate or find an alternative white knight acquirer beforehand. At least these days it is a white knight – back in the 1980s targets were much more creative with crown jewel sales, Pac-Man defenses and leveraged recapitalizations. But the wild 1980s are over, and shareholder pressure acts to prevent these more aggressive responses. In particular, the travails of Yahoo have shown that a “just say no” strategy can leave the target without a bidder and a severely damaged business.

This is why the staggered board is so controversial. A company with a staggered board has only one-third of its directors up for election in any given year. By requiring a hostile bidder to run two proxy contests in two years to force a transaction, the staggered board appears to discourage bidding, a deterrent that is not compensated for by higher share premiums. Lucian A. Bebchuk, John C. Coates and Guhan Subramanian of Harvard Law School have conducted empirical research on bids from 1996 to 2000 that confirms this finding.

Still, anecdotally at least, there is some counter-evidence. In two more recent short-slate contests — Weyerhaeuser’s acquisition of Willamette Industries and AirTran Holdings’s failed acquisition of Midwest Air Group — the bidder elected a short slate of directors. The companies were subsequently forced to enter into a change of control transaction.

While the jury is still out, I personally believe that a staggered board does deter bidding, although the increased shareholder pressure these days is diminishing the impact of this anti-takeover device.
But two recent transactions have chosen strategies counter to what I thought was the standard practice in a hostile of pairing a proxy contest with an offer. These two are Agrium’s unsolicited offer for CF Industries and Astellas’s hostile offer for CV Therapeutics.

Agrium’s conduct is the odder and less explainable one. CF has a staggered board, but even then Agrium announced their bid after the Feb. 12 nomination deadline to nominate directors to replace a third of this board (a so-called short-slate proxy contest). Even if Agrium is only willing to act on a friendly basis, I can’t understand why Agrium would forgo the pressuring option of a proxy contest. I have no further information but can only speculate that it was a mistake or that they couldn’t get their act together in time. Alternatively, perhaps Agrium believes that the short-slate proxy contest is simply that, a way to force a board to act under shareholder pressure. In that case, if Agrium believes that shareholder pressure is all it needs, then perhaps a well-priced bid would win the day if CF resisted.

The shareholder pressure route is the rational explanation, so maybe their conduct is indeed an endorsement of the new shareholder activism and its effects.

This explanation for Agrium’s decision is at least partially endorsed by Astella’s conduct. Astella’s hostile represents a trend. Last year there were at least three hostiles by Japanese companies and according to Dealogic, Japanese deals amounted to $36 billion. The hostile trend is particularly noteworthy because it goes against the historic perception that Japanese companies were unwilling to engage in such overt hostile conduct.

Astellas delivered its bear hug on Jan. 27 offering $16 a share in cash. CV rejected the offer on Feb. 20 in a standard statement that “[t]he board, with the assistance of its financial and legal advisors, has carefully considered your proposal to acquire our company in the context of our strategic plans and the best interests of our stockholders. We concluded that your proposal significantly undervalues CV Therapeutics and its potential growth opportunities and we decline to accept it.” Ho hum.

Also on that date, CV amended its poison pill trigger to pick up derivative transactions. This act is in and of itself is a response that I haven’t seen before and likely due to the standstill Astellas has with CV (more on that below). CV also amended its bylaws to include enhanced notification provisions for anyone wishing to initiate a proxy contest (read Astellas).

Astellas launched a cash tender offer on Friday. The offer’s conditions are broad but not as broad as they could be. The offer requires that the CV board consent to the offer and that the CV board remove CV’s poison pill restrictions. There is no financing or due diligence condition.

Still, there is one condition here that is interesting, a standstill condition. Astellas entered into a standstill with CV on July 10, 2000 in connection with the licensing by Astellas of certain of CV’s products. The standstill states: “[u]ntil the first anniversary of the expiration or termination of the License Agreement, [Astellas] shall not purchase and shall ensure that none of its Affiliates purchases, any Common Stock [of CV] other than the purchase or acquisition of Shares contemplated by this [Stock Purchase] Agreement.”
The offer is conditioned on CV waiving the standstill requirement. Frankly, it is a bit odd that this standstill is so narrow — typically a standstill also excludes even the making of a proposal to acquire the company. Once again, the importance of the details is emphasized to lawyers.

But as for a proxy contest, Astellas forewent this option instead preferring to state that “[t]he Company also announced that it is considering taking action in connection with CV Therapeutics’ 2009 Annual Meeting.” Here, CV has a staggered board. The reluctance of Astellas to launch a proxy contest now may reflect the problem of dealing with a staggered board. For now, Astellas is content to let shareholder pressure work with the proxy contest a threat.

Per CV’s last proxy statement, the nomination deadline for CV directors is no later than the close of business on March 21, and no earlier than the close of business on Feb. 19, 2009. CV can postpone the meeting and the nomination deadline though to buy some time. Considering their conduct thus far, this is likely, though Delaware law limits how far the target can postpone the annual meeting to thirteen months after the last one.

In any event, 10 percent of the voting power of CV can call a special meeting. Uniquely, CV allows for the removal of directors at this meeting, but this would require a 66 2/3 percent vote. So, Astellas can try and call a meeting to remove the full board, but the shareholder vote it would require is quite high. It is therefore more likely to start with a simple short-slate proxy contest.

The end result is that Astellas’s latest move is merely a raising the pressure upon CV. Like a fisherman releasing tension in his line, Astellas is waiting for CV’s response before trying to further reel the company in. This is more explainable conduct than Agrium’s and may be a sign of the new world of shareholder activism. In other words, it may be that a proxy contest is important, in a hostile but the threat thereof is sufficient in this market, even with a staggered board in place.

The truth remains to be seen. –Steven M. Davidoff