

Breakingviews: Chesapeake Could Use a Fresh Start in a New Home

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Chesapeake Energy could use a fresh start in a new home. The embattled U.S. gas producer faces a shareholder vote next month to incorporate in Delaware. The board's argument that stiff takeover defenses in Oklahoma, where its headquarters are now, better serve investors is a stretch. Chesapeake needs a governance overhaul. A new legal address would be a good first step.

Such a move would also be a homecoming. Chesapeake was a Delaware corporation until it relocated in 1996. It said then that it wanted to save \$200,000 in franchise taxes, though its annual revenue was \$150 million.

The real payoff came much later, when Chesapeake helped draft a 2010 Oklahoma law requiring big public companies to put only a third of their boards up for election each year. Chesapeake spurned shareholder requests in 2008 and 2009 for annual director elections that would have made overhauling the board easier.

Entrenching a so-called classified board puts Chesapeake out of step with about three-quarters of the S&P 500. This proxy season, dozens more corporations have agreed to declassify. The evidence isn't clear-cut, but research by Harvard Law School's Lucian Bebchuk and Alma Cohen shows companies with annual elections fetch higher valuations.

Chesapeake's board hardly merits extra protection anyway. It presided over Chief Executive Aubrey McClendon's risky deal-making and borrowing, which have put the company under the spotlight. Its market value has tumbled 40 percent over the last five years compared with significant gains by rivals EOG Resources and Range Resources.

Though Delaware's laws are very similar to Oklahoma's, the First State allows classified boards only with shareholder authorization. Delaware also makes it easier for owners to amend company bylaws. And its courts have deep experience resolving corporate disputes.

Chesapeake opposes the change, saying the classified board deters unwanted predators and that directors have already complied with shareholder demands to lower CEO and board compensation and elect directors by a majority of votes cast rather than a plurality. It also says Oklahoma courts will give the company a fairer shake.

But Oklahoma's enthusiasm for the 2010 law suggests that management and the state legal establishment may already be too close. Given Chesapeake's troubles, a new beginning in Delaware might do shareholders some good.

CONTEXT NEWS

- Chesapeake Energy shareholders are scheduled to vote on June 8 on a proposal to change the company's state of incorporation from Oklahoma to Delaware. Supported by investors such as New York State Comptroller Thomas DiNapoli, who oversees \$140 billion in state pension funds, the proposal seeks to get around certain state laws, including one that prevents public companies with over 1,000 stockholders from putting more than a third of their board of directors up for election each year.

- The Chesapeake board opposes the proposal, arguing that reincorporating in Delaware would be expensive and deprive the company of useful takeover defenses as well as favorable treatment by courts in Oklahoma, where Chesapeake has its headquarters. (Reporting by Reynolds Holding, a Reuters Breakingviews columnist. The opinions expressed are his own.)