Conference Tackles Role of Shareholder Activism

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How much control should the "owners" of U.S. corporations exercise? That was one of the underlying questions as attorneys, academics and investors gathered for a conference on shareholder activism.

About 175 people attended the Manhattan conference, the sixth such event organized by the Institutional Investor Educational Foundation. Last year's conference drew about 125 participants.

Interest in the event reflected a growing push by large investors, including aggressive hedge funds, to influence the management of companies so as to achieve the best possible return on their money.

One panel discussion focused on "Shareholders or Directors: Who's in Charge Here?"

"Ownership rights need to be preserved to hold directors [accountable] as agents," said panelist Richard Ferlauto, director of corporate governance and pension investment for the American Federation of State, County and Municipal Employees (AFSCME)

Lucian Bebchuk, a professor at Harvard Law School, said that shareholders should have access to "the rules of the game that regulates boards and directors" by being able to amend company bylaws.

Bebchuk has presented reform measures to the annual meetings of several large corporations, including Long Island, N.Y.-based CA.

However, panel participant Trevor Norwitz, a partner at Wachtell, Lipton, Rosen & Katz, defended the present system in which shareholders rely on directors to set policy.

Norwitz noted that the U.S. has become the "growth engine of the world" by sticking with this model, but "people are trying to turn it on its head."

He also said there was no need for the radical reforms sought by activists.

Norwitz said there has been a "dramatic shift" toward empowering boards to do the "right thing" by protecting shareholders since the Enron and WorldCom scandals.

"It used to be the case that when an activist shareholder came forward, a company's instinct would be to tell them to go jump in the lake," he said. "That has changed."

As a result, he said that shareholders have "added value" to their investments.

Moreover, Lawrence A. Hamermesh, a professor at Widener University School of Law, said that giving shareholders more say over corporate governance could create uncertainty.

"If you change the rules, you create a situation where you don't know how the different people are going to act," he said.

Ferlauto of AFSCME said in an interview that "activism" means that institutions are acting more and more like owners of the companies in which they have stock.

"They work to hold boards of directors accountable for their actions," he said.

Stuart Grant of plaintiffs firm Grant & Eisenhofer, the law firm sponsor of the event, said in an interview that the tug of war really involved "capital vs. management."

Norwitz of Wachtell noted that the activists themselves are varied. Some are hedge funds, while others are pension funds of trade unions.

Two days before the conference, the Securities and Exchange Commission passed a rule granting companies the authority to deny shareholders access to the proxy ballots they send to shareholders. In doing so, the SEC action was an attempt to address a ruling by the 2nd U.S. Circuit Court of Appeals in American Federation of State, County and Municipal Employees v. American International Group, 462 F. 3d 121.

The SEC's move was not brought up at the panel discussion, but afterward, Ferlauto, whose organization was the plaintiff in the 2nd Circuit case, called the SEC's rule "ill considered." He said that since the rule was issued his union has asked the boards of Bear Stearns and JPMorgan Chase to provide it with access to their ballots.

Grant, whose firm represented AFSCME, said the SEC's action was "a very bad one for shareholders and corporate democracy."

But Norwitz called the SEC's rule "a rare victory for the forces of sanity in this activist world."

HEDGE FUND ACTIVISM

Hedge funds have been blamed -- or praised -- for much of the current wave of activism. Among other things, they have pushed for seats on company boards and lobbied hard for changes in business strategies.

"Hedge funds want a seat on the board and want to control the board," said April Klein, a professor at New York University's Stern School of Business, who participated in a panel on hedge fund activism. "They are not afraid to start a proxy fight."

The proxy contest waged earlier this year in part by hedge fund SAC Capital Advisors against the management of Take-Two Interactive Software is just one example.

Randall Thomas, a professor at Vanderbilt University School of Law, agreed that "hedge funds are willing to spend the money [on proxy fights], and that is unusual."

Klein and Thomas have conducted separate studies on the impact of activist hedge funds, and both concluded that the hedge funds' actions have had a positive impact on shareholders and the economy.

See Klein's study and Thomas' study.

Thomas said there was "clear evidence" that the intervention of a hedge fund leads to a jump in stock prices for a targeted company. He also said that the way a company operates improves and chief executive officer pay decreases.

Panel participant Kenneth Altman, president of the proxy solicitation company The Altman Group, agreed that as a result of hedge fund activism, managers have become more thoughtful, especially in the cases of mergers, and that their advocacy is positive for investors.

ALM Events, an affiliate of the New York Law Journal, coproduced the conference.