THE SHAREHOLDER RIGHTS AND ACTIVISM REVIEW

EIGHTH EDITION

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PREFACE

In the years since the financial crisis, shareholder activism has been on the rise around the world. Institutional shareholders are taking a broad range of actions to leverage their ownership position to influence public company behaviour. Activist investors often advocate for changes to the company, such as its corporate governance practices, financial decisions and strategic direction. Shareholder activism comes in many forms, from privately engaging in a dialogue with a company on certain issues, to waging a contest to replace members of a company's board of directors, to publicly agitating for a company to undergo a fundamental transaction.

Although the types of activists and forms of activism may vary, there is no question that shareholder activism is a prominent, and likely permanent, feature of the corporate landscape. Boards of directors, management and the markets are now more attuned to and prepared for shareholder activism, and engaging with investors is a priority for boards and management as a hallmark of basic good governance.

Shareholder activism is a global phenomenon that is effecting change to the corporate landscape and grabbing headlines around the world. Although shareholder activism is still most prevalent in North America, and particularly in the United States, activism campaigns directed at non-US companies now represent approximately half of global activism activity. This movement is being driven by, among other things, a search by hedge funds for diversified investment opportunities and a cultural shift towards increased shareholder engagement in Europe, Australia and Asia.

Boosted by record activity levels in the first quarter of 2022, global activism activity has returned to pre-pandemic levels despite continued market volatility and uncertain macroeconomic conditions. Looking forward, activism activity is generally expected to remain strong, particularly in Europe and Asia, and shareholder activists are expected to remain focused on environmental, social and political considerations and corporate governance as well as company operating performance.

As shareholder activists and the companies they target continue to be more geographically diverse, it is important for legal and corporate practitioners to understand the legal framework and emerging trends of shareholder activism in the various international jurisdictions facing activism. *The Shareholder Rights and Activism Review* is designed to be a primer on these aspects of shareholder activism in such jurisdictions.

My sincere thanks go to all of the authors who contributed their expertise, time and labour to this eighth edition of *The Shareholder Rights and Activism Review*. As shareholder activism continues to diversify and increase its global footprint, this review will continue to serve as an invaluable resource for legal and corporate practitioners worldwide.

Francis J Aquila
Sullivan & Cromwell LLP New York
August 2023

Chapter 16

UNITED STATES

Francis J Aquila and Lauren S Boehmke[1]

I OVERVIEW

Shareholder activism is and will continue to be a prominent feature of the corporate landscape in the United States. Following a wave of corporate scandals in the early 2000s (most memorably Enron Corporation), there was a sea change in US corporate governance. Subsequently enacted federal regulations that focus on corporate governance have dramatically changed the face of US corporate boards of directors; shareholder engagement has become an expectation for companies; and a number of other legal and cultural changes have increased the power of shareholders of US public companies.

Shareholder activism historically referred to an asset class of hedge funds that raided and agitated US publicly traded companies. In present times, however, there is broader recognition that shareholders more generally have a desire to engage with management and boards of directors regarding governance reforms and other aspects of a company's business. This trend has caused the lines between the traditional shareholder activists and other shareholders of public companies to blur, thereby diluting the brand of shareholder activism. There is now an increased expectation that shareholders will seek to have more influence over governance and strategic decisions made by public companies, although it is still the case that certain activist campaigns become a public display of the differences of strategic vision between the shareholder activist and its subject company.

Although the term 'activist' may have become diluted by more types of shareholders entering the mix, the increased acceptance of activism in the corporate landscape has by no means decreased its frequency. As at 2019, the total number of activist campaigns had been remarkably consistent over the prior five years.[2] While activist campaigns declined during 2020, largely because of the covid-19 pandemic, since that time, the number of shareholder activism campaigns against US public companies has generally returned to pre-pandemic levels.[3] However, US activity levels have been less robust in 2023, down 34 per cent in the first quarter as compared with Q1 2022.[4]

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1 Francis J Aquila and Lauren S Boehmke are partners at Sullivan & Cromwell LLP.

2 For further information, refer to the Sullivan & Cromwell LLP publication '2022 U.S. Shareholder Activism and Activist Settlement Agreements', dated 13 December 2022 (S&C 2022 Shareholder Activism Review), available at https://www.sullcrom.com/SullivanCromwell/_Assets/PDFs/Memos/sc-publication-2022-us-shareholder-activism-review.pdf, at pp. 1 and 10.

3 id., at pp. 1, 5 and 10.

4 See Lazard Capital Markets Advisory Group, 'Shareholder Activism Update: Early Look at 2023 Trends' (Lazard Shareholder Activism 2023 Trends), available at https://www.lazard.com/research-insights/shareholder-activism-update-early-look-at-2023-trends/.

In any event, the statistics for public campaigns do not tell the entire story: for every public activist demand, there may be another activist campaign that never becomes public knowledge. Success by activist hedge funds in raising capital and increased support from prominent institutional investors, combined with activists achieving their objectives and gaining board seats at public companies (through both settlements with companies and proxy contests), has fuelled increased activity. As a result, US public company boards of directors and management teams have continued their focus on understanding shareholder activism as well as working to prevent, and preparing to respond to, activist campaigns.

II LEGAL AND REGULATORY FRAMEWORK

The legal and regulatory framework relating to shareholder rights, activism and engagement in respect of US publicly traded companies primarily comprises federal laws and regulations and state corporations laws. US public companies also must comply with the Listing Rules of their stock exchange (either the New York Stock Exchange or the Nasdaq Stock Market), which include corporate governance requirements. Additional sources of practice with respect to shareholder activism and engagement include proxy advisory firms and guidelines set forth by other investment community members. Taken together, the applicable laws and regulations, as well as other influential sources of practice, govern the means by which a shareholder activist pursues an activist campaign and the structural defences against shareholder activists available to US public companies.

i Federal laws

Federal securities laws relating to shareholder activism and engagement include the Securities Act of 1933, the Securities Exchange Act of 1934 (the Exchange Act), the Sarbanes-Oxley Act of 2002 and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the Dodd-Frank Act). The federal securities laws, and the rules and regulations promulgated thereunder, are administered by the Securities and Exchange Commission (SEC). A key focus of the federal securities regulations is on disclosure and ensuring that shareholders and the market have the information required to make fully informed investment decisions.

The Exchange Act provides the SEC with broad authority to regulate the securities industry. Pursuant to Section 13(a) of the Exchange Act, the SEC requires periodic and current reporting of information by public companies, and companies must consider these disclosure requirements in reporting on corporate governance matters. Section 13(d) of the Exchange Act requires reporting by persons who have directly or indirectly acquired beneficial ownership of more than 5 per cent of an outstanding class of a company's equity securities. An activist investor that crosses the 5 per cent threshold must file a report with the SEC within 10 calendar days disclosing its ownership and certain additional information, including its activist intentions. Section 13(d) also governs whether investors are considered a 'group' for purposes of acquiring, holding or disposing of a company's securities, a relevant consideration for shareholder activists who may form a 'wolf pack' to work together on an activist campaign.

Section 14(a) of the Exchange Act imposes disclosure and communications requirements on proxy solicitations or the materials used to solicit shareholders' votes in annual or special meetings held for the election of directors and the approval of other corporate actions. Shareholder activists that wage a proxy contest to nominate directors for election in opposition to a company's slate of director nominees must comply with these proxy solicitation rules. These rules apply to, and require the timely filing of, all written communications made as part of the solicitation, including press releases, investor presentations, transcripts of speeches and certain interviews, and social media postings. Further, the Exchange Act governs disclosure by anyone seeking to acquire more than 5 per cent of a company's securities by means of a tender offer.

Regulation Fair Disclosure (Regulation FD), which aims to promote full and fair disclosure by ensuring that companies do not engage in selective disclosure, requires a public company to make public disclosure of any material non-public information disclosed to certain individuals, including shareholders, who may trade on the basis of that information. Regulation FD applies to discussions between a company and a shareholder activist; therefore, companies must be mindful of this Regulation when holding discussions with an activist.

The Sarbanes-Oxley Act, enacted in response to the corporate scandals in the early 2000s, mandated numerous reforms to enhance corporate responsibility and financial disclosures. The Dodd-Frank Act implemented further reforms, including with respect to trading restrictions, corporate governance, disclosure and transparency. Both statutes have had a significant influence on corporate governance and shareholder activism and engagement.

In addition to the federal securities laws, the Hart-Scott-Rodino Antitrust Improvements Act (the HSR Act) may apply to an investment by a shareholder activist in a public company if the investment exceeds a certain size threshold, currently set at US$111.4 million for 2023.[5] If an activist will cross the size threshold with respect to the amount of voting securities of a company it intends to acquire, the activist is required to make a filing with US antitrust authorities and observe a waiting period prior to completing the transaction. The HSR Act provides an exemption from reporting requirements for acquisitions that result in the acquirer holding 10 per cent or less of a company's outstanding voting securities if made 'solely for the purpose of investment'.[6] This investment-only exception has been construed narrowly; it does not apply if an investor intends to participate in and influence business decisions, which is often the case with shareholder activists.[7] In July 2016, activist hedge fund ValueAct Capital agreed to pay a record US$11 million fine to settle a lawsuit filed by the US government alleging that ValueAct violated the HSR Act by improperly relying on the investment-only exception in connection with its US$2.5 billion investment in Halliburton Company and Baker Hughes Inc.[8]

5 The current threshold, which is adjusted annually for inflation by the Federal Trade Commission, is available at www.ftc.gov/enforcement/premerger-notification-program/current-thresholds.

6 See 15 U.S.C. Section 18a(c)(9) and 16 C.F.R. Section 802.9.

7 See 43 Fed. Reg. 33,450, 33,465 (1978).

8 See US Department of Justice press release 'Justice Department Obtains Record Fine and Injunctive Relief against Activist Investor for Violating Premerger Notification Requirements', dated 12 July 2016.

ii State laws

State corporations law governs actions by companies in the state's jurisdiction and establishes the fiduciary duty regime that applies to a company's directors and officers. This chapter focuses on corporate law in the state of Delaware because it is the most popular state of formation for legal entities and its laws significantly influence corporate law in other states. Many provisions of the Delaware General Corporation Law (DGCL) govern the relationship between a corporation and its shareholders and have an impact on the processes by which a shareholder activist may pursue, and a company may defend against, an activist campaign.

The DGCL includes laws governing, among other things, the composition of the corporation's board of directors, annual and special meetings of shareholders, actions by written consent, voting thresholds for approving corporate actions, requests by shareholders for books and records, and appraisal rights. As described further in Section II.iv, a corporation may use its organisational documents (certificate of incorporation and by-laws) to customise certain elements of its corporate governance to the extent not inconsistent with the DGCL.

All directors and officers of Delaware corporations owe the company and its shareholders fundamental fiduciary duties of care, loyalty and good faith. Subject to certain exceptions, when reviewing a company's decision, the Delaware courts apply the 'business judgement rule', which presumes that directors satisfied these fiduciary duties, and will not second-guess the directors' decision if it has a rational business purpose. However, enhanced judicial review applies in certain circumstances, including when a board of directors takes defensive measures in response to a perceived threat to corporate control. Under the *Unocal* test,[9] a board that has implemented a defensive measure has the burden of demonstrating that it had reasonable grounds to believe that a threat to corporate policy and effectiveness existed, and that its defensive response was reasonable in relation to the threat posed. The *Unocal* test is particularly relevant to shareholder activism because it applies to defensive measures such as shareholder protection rights plans (poison pills). Shareholder activists may, as part of their campaign strategy, file lawsuits against a corporation and its directors and officers alleging fiduciary duty violations. In November 2021, the Delaware Supreme Court upheld the Delaware Chancery Court's ruling to strike down the Williams Companies' rights plan.[10] The Delaware Chancery Court applied the *Unocal* intermediate enhanced scrutiny standard and held that the Williams board conducted a good faith, reasonable investigation in adopting the rights plan, but it cast doubt on some of the threats underpinning the rights plan and found that Williams' response was not proportional to the stated threats. Williams enforces that a board is required to define specific and viable threats, narrowly tailor shareholder protection rights plans to those threats, and memorialise its decisions in a clear and thorough record.

iii Additional sources of practice

Shareholder activism and engagement are influenced by other sources of practice and various members of the investment community. Although their impact has waned somewhat in recent years, proxy advisory firms such as Institutional Shareholder Services (ISS) and, to a lesser extent, Glass Lewis have an impact on a company's corporate governance policies and may affect the outcome of a proxy contest with a shareholder activist. These advisory firms

9 *Unocal Corp v. Mesa Petroleum Co* 493 A.2d 946 (Del. 1985).

10 *The Williams Cos. Stockholder Litig.*, C.A. No. 2020-0707-KSJM, 2021 WL 754593 (Del. Ch. Feb. 26, 2021); *aff'd, The Williams Cos. v. Wolosky*, 264 A.3d 641 (Del. 2021).

set forth policy guidelines as well as make recommendations with respect to proposals to be voted on at a shareholders' meeting, such as director elections, fundamental transactions and other governance matters. As an adviser to many institutional shareholders, ISS is keen on shareholder engagement and is often inclined to take a 'what's the harm' approach and recommend in favour of at least one activist director candidate in a proxy contest for minority representation on the board of directors if the shareholder activist has demonstrated that some change is warranted at the company. ISS recommendations match the ultimate outcome of the vote in a majority of proxy contests. Although the gap between the voting practices of ISS and institutional shareholders has narrowed, large traditional institutional investors such as BlackRock, Fidelity, State Street and Vanguard have generally stopped relying on the analysis of proxy advisory firms and have instead developed internal proxy advisory functions to make decisions in proxy contests and put forth corporate governance initiatives. Given that the stock ownership of many US public companies is increasingly held by a relatively small number of these large institutions, it is critical for both the company and the shareholder activist to garner the support of these investors. Other members of the investment community, such as the Teachers Insurance and Annuity Association of America-College Retirement Equities Fund, the California State Teachers' Retirement System and the Council of Institutional Investors, also set forth policy guidelines and express opinions on governance and activism.

iv Company defences

A company's best defence against shareholder activism is strong financial performance, a solid record of shareholder engagement and adoption of corporate governance best practices. A company must also adopt a proactive strategy to anticipate and prepare for the potential for an activist campaign, including actively monitoring the company's shareholder base and conducting regular and thorough reviews of the company's business plan, strategic alternatives and intrinsic value. In the current environment, in which there is now an expectation that shareholders will be more involved in governance and strategic decisions made by public companies, it is crucial for companies to maintain a positive dialogue, relationship and credibility with its shareholders, particularly key institutional investors and other large holders. Practising consistent shareholder engagement, including articulating the company's current and long-term vision for creating shareholder value and practising good governance, will pay dividends for the company in terms of both understanding investor concerns and securing support in the face of future shareholder activism campaigns. A shareholder activist may face an uphill battle if the company already has a strong relationship with, and the support of, its large institutional shareholders.

The prevalence of shareholder activism in the United States has created an entire cottage industry of firms, such as proxy solicitors, dedicated to helping companies monitor their shareholders and set up meetings with institutional investors. Investment banks and law firms also have groups of professionals dedicated to activist preparation and defence. A company facing an activist investor requires a core response team of outside advisers, including a law firm, proxy solicitor, investment bank and public relations firm. The most prepared companies create these teams in advance and establish procedures that are ready to be implemented on a moment's notice should an activist appear. In addition to monitoring a company's shareholders and facilitating shareholder engagement, a company's adviser team can assist the company with 'thinking like an activist' by routinely assessing the company's

strengths and vulnerabilities to activism, reviewing its structural defences and keeping current on the evolving corporate governance practices and preferences of its shareholders and the broader market.

Companies have structural governance defences that may protect them against shareholder activists. The value of any particular structural defence will depend on the specific activist situation, and no defence will fully protect a company against activism. As mentioned above, a company may customise certain governance elements in its organisational documents. For example, most public companies have by-laws that require a shareholder to provide advance notice and certain information to the company before it is permitted to nominate a director for election to the company's board of directors or propose business before a shareholders' meeting, and these by-laws eliminate the possibility of surprise from last-minute proposals. Companies also specify in their by-laws that the board of directors has the sole right to determine its own size and fill vacancies, both of which prevent activist shareholders from filling the board of directors with their preferred candidates. Companies may also restrict its shareholders' ability to call special meetings or take actions by written consent either entirely (which is becoming less common) or below certain ownership thresholds.

Some companies have adopted even more stringent structural defences, such as having two classes of stock (one of which has additional voting rights and is not publicly traded, limiting an activist's ability to obtain voting power) or creating a classified board of directors (directors are divided into three classes with staggered, multi-year terms, making it more difficult for an activist to replace board members). Companies may also adopt a poison pill, which can be triggered by the company to dilute the equity and voting stake of a shareholder that has purchased over a certain percentage of the company's stock by allowing all other shareholders to purchase additional shares at a steep discount. Most large US companies have abandoned these harsher defences in light of scrutiny from the institutional investor community and proxy advisory firms. It is recommended that companies keep a rights plan 'on the shelf' and ready to be implemented in response to a threat from a particular activist (see the *Unocal* defensive measures discussion in Section II.ii), although the company must weigh the possibility that the market may react negatively even if it successfully blocks an activist campaign. In 2022, likely in response to the volatile market environment, an increasing number of companies adopted rights plans in an effort to pre-empt hostile takeovers or activist campaigns.[11]

The DGCL Section 203 includes an anti-takeover provision that prevents a corporation from entering into certain business combination transactions with an interested shareholder (generally one that owns more than 15 per cent of the company's stock) for three years after becoming an interested stockholder unless the business combination is approved in the manner prescribed by the statute.

The HSR Act requires an investor to provide written notice to a company before acquiring shares that are subject to the HSR Act's filing requirements, which may serve as the first warning to the company that an activist intends to take a significant stake in the company and advocate for change, or alternatively that an existing shareholder has altered its intentions with respect to the company from passive to active and plans to increase its stake.

11 S&C 2022 Shareholder Activism Review, at pp. 5 and 6.

III KEY TRENDS IN SHAREHOLDER ACTIVISM

i Shareholder activists

Shareholder activists primarily fall into two categories: hedge fund activists and Rule 14a-8 activists. Hedge fund activists are investors whose investment strategy is to identify what they consider to be vulnerabilities at certain companies and purchase a sizeable minority stake in those target companies with the view that changes they recommend and agitate for, if successful, will increase shareholder value and result in a financial gain for their investment portfolio. Rule 14a-8 activists are shareholders that submit proposals to companies under Rule 14a-8 promulgated under the Exchange Act, a Rule that requires a public company to include a shareholder proposal in its proxy materials for a shareholders' meeting if certain requirements are met by the shareholder. A company's preparation for and response to activism will differ depending on the type of shareholder activist it faces.

Hedge fund activists are the main focus of this chapter. Each hedge fund activist has its own strategy, objectives, personality and frequency of engaging in activism. Some activists, such as Carl Icahn and Trian, are long established, while others are second generation. The investment horizon of an activist hedge fund can range from very short-term to somewhat longer-term. Certain hedge fund activists invest their own funds, whereas others invest third-party funds. Additionally, an activist hedge fund's redemption policy (e.g., whether investors have the right to redeem their funds quarterly or have longer-term 'lock-up' commitments) may have an impact on its behaviour and investment strategy.

Rule 14a-8 activism is often socially driven, with the activists including retail shareholders, advocates of social issues (e.g., environmentalists), religious organisations, pension funds and a variety of other groups. During the 2022 proxy season, submissions on environmental, social and political (ESP) topics continued to increase and represented 63 per cent of proposals submitted through H1 2022, led by a 38 per cent year-over-year increase in environmental proposals.[12] However, support for ESP proposals fell during H1 2022, breaking a trend of increasing support over the past 10 years.[13] The vast majority of Rule 14a-8 proposals are targeted at S&P 500 companies.[14] Traditional institutional investors such as BlackRock, Fidelity, State Street and Vanguard may be considered shareholder activists as well. The percentage ownership of public companies among these large institutional investors is significant. These institutions have developed internal proxy advisory functions and are displaying an increased willingness to directly express their views on governance matters in recent years. These investors are long-term shareholders by nature, and their inability to exit investments nimbly increases their incentive to advocate for changes that will increase enterprise value and protect their investment. However, the emergence of 'pass-through voting' by these institutions, which allows certain of their underlying investors to choose how to vote on corporate matters, may make voting outcomes less predictable.[15] Traditional institutional investors also increasingly support activism, although in certain cases there may be a tension between the institutional investor's long-term outlook and a shareholder activist's short-term focus.

12 For further information, refer to the Sullivan & Cromwell LLP publication '2022 Proxy Season Review: Part 1', dated 8 August 2022 (S&C 2022 Proxy Season Review), available at https://www.sullcrom.com/SullivanCromwell/_Assets/PDFs/Memos/sc-publication-2022-Proxy-Season-Part-1-Rule-14a-8.pdf, at p. 1.

13 id., at pp. 1–4.

14 id., at p. 6.

15 S&C 2022 *Shareholder Activism Review*, at p. 11.

In recent years, there has also been a noticeable blending of investment strategies by investors with historically distinct investment strategies, particularly activist hedge funds and private equity firms. While certain activist investors such as Paul Singer of Elliott Capital Management (Elliott) and Carl Icahn have long been selectively acquisitive due to their size, other activist investors are also employing private equity-like strategies. For their part, some private equity firms have recently taken up their own form of activist investing, including acquiring minority stakes. Despite their historical differences, private equity firms and hedge funds share a common ultimate objective of acquiring an ownership stake in a company they consider to be undervalued, effecting certain changes at the company designed to boost value, and then realising a return on their original investment by exiting the company at a higher valuation. Other traditionally passive investors could also move towards an activist approach, paving the way for a further convergence of investment strategies.

ii Target companies

Hedge fund activists target companies in which they think there is potential to increase shareholder value, and often look for traditional red flags such as stock price underperformance, operational challenges relative to peers, significant unused cash on the balance sheet, perceived management weakness, multiple business lines, undervalued assets or perceived excessive executive compensation. However, shareholder activists also target companies that have performed in line with or better than their peers. A company's liquidity and size of its market cap can play a role in its susceptibility to activism; it is inherently more difficult for a shareholder activist to amass a large enough stake to influence a company with illiquid stock or a large market cap. Nevertheless, activists have been successful with small stakes (under 1 per cent) and have targeted even the largest and most well-run companies, proving that no company is immune to activism. In 2022, there were more campaigns targeting issuers with market caps above US$1 billion than in prior years.[16]

iii Activist campaigns

The general consistency of the data in recent years (other than 2020, which was impacted by the covid-19 pandemic) suggests that activism will continue to be an important consideration for companies going forward. Shareholder activists pursue a variety of objectives, including pursuing a company's sale to a third party (or, conversely, seeking to block a planned merger); pushing for another type of fundamental transaction, such as a spin-off; balance sheet demands such as dividends or share repurchases; operational and capital structure demands; and governance and ESP demands. Shareholder activists frequently pursue multiple objectives in the same campaign, with governance demands – particularly board representation or seeking changes in management – often used as a means of achieving economic objectives. Activists in 2022 increasingly focused on ESP, corporate strategies, and operations and management changes, shifting away from M&A-related campaigns due to market conditions.[17]

Shareholder activists utilise a number of different strategies to achieve their objectives, depending on factors such as the activist itself (many have a consistent modus operandi) and the subject company's defensive posture. The standard activist 'playbook', though not applicable to every campaign, follows a series of escalating tactics with the key objective

16 id., at p. 10.

17 id., at pp. 5, 7 and 8.

of creating an impression of inevitability. A shareholder activist often begins a campaign by engaging in a private dialogue with the company's management before its stake in the company becomes public. If successful, these discussions can avoid further agitation by leading to either an informal or a formal settlement between the company and the shareholder activist. If private discussions fail, the shareholder activist may initiate a public campaign to apply pressure on the company through press releases; open letters to management, the board of directors and shareholders; issuing white papers presenting its investment thesis and analysis; and using other means of communication to rally the company's other shareholders to support its cause. Shareholder activists are also adept at using media, including social and alternative electronic media, to their advantage.

The shareholder activist may then threaten and eventually initiate a proxy contest for representation on the company's board of directors. Shareholder activists seek to gain representation by either replacing only a minority of the company's directors or, in more extreme – but not less common – scenarios, trying to replace at least a majority of the board of directors (a control slate contest). If a shareholder activist is well funded, it may also commence a lawsuit (sometimes in conjunction with other tactics) to obtain information from the company, reverse board decisions or redeem the company's poison pill, among other claims. As discussed further in Section III.i, shareholder activists do not usually make an offer for the entire company, but hostile offers have been made by hedge fund activists in past campaigns.

iv Paths to resolution

Activist campaigns have generally continued to achieve high levels of success in recent years, although activists achieved less success than usual in 2021.[18] Shareholder activists place a high value on the public perception of a successful campaign, including a partial victory or settlement, even without achieving an outright win for all of its demands. Partial success can entail the shareholder activist receiving at least one board seat (through either a settlement or a proxy contest that goes to a vote) or the company agreeing to pursue one of the activist's economic objectives.

It is common for a company and shareholder activist to settle and enter into a cooperation agreement. A typical cooperation agreement provides the shareholder activist with minority board representation and includes customary standstill restrictions for the benefit of the company, such as prohibiting the activist from soliciting proxies in opposition to management prior to the company's next annual meeting. In many cases, companies conclude that settling with a reputable activist is preferable to expending significant time and resources on a protracted and distracting proxy contest. A company's board of directors has an interest in appearing firm but open-minded about an activist's credible suggestions to its other shareholders and the investment community at large. Most shareholder activists also have an interest in creating working relationships with the company's board of directors and building a public reputation for playing fair, which can facilitate future negotiations with the company and the future subject companies.

18 id., at p. 12.

Companies must recognise that providing a shareholder activist with board representation is simply the beginning and not the end of the company's discussions with the activist. Once the shareholder activist is represented on the board of directors, it will most likely seek changes that it believes are in the best interests of the company and its shareholders. In addition, the presence of the activist's director designees may alter boardroom dynamics. Activist designees that receive board seats also stay on the boards for long periods. Since 2010, prominent activist fund insiders who became directors following a settlement agreement stayed on the relevant board for an average of approximately 31 months longer than the minimum provided for in the settlement agreement, and many insiders in this subset are still on the relevant board.[19]

IV RECENT SHAREHOLDER ACTIVISM CAMPAIGNS

Although there are many recent US shareholder activism campaigns worthy of discussion in this chapter, this section highlights two campaigns by US activist hedge funds against US public companies that helpfully demonstrate the varying nature and objectives of shareholder activists.[20]

i Illumina/Icahn

In March 2023, Icahn disclosed ownership of approximately 1.4 per cent of gene sequencing company Illumina, Inc and initiated a proxy contest to elect three director nominees, all current or former Icahn associates, to Illumina's board of directors at its 2023 annual meeting. Icahn primarily objected to Illumina's completed acquisition of cancer detection test maker Grail LLC, citing a lack of global antitrust approval for the deal, and urged Illumina to replace its CEO and unwind the Grail acquisition. Following a months-long public proxy battle in which Illumina defended its Grail acquisition and criticised Icahn's lack of understanding of its business, in May 2023, Illumina shareholders voted at the annual meeting to elect one of Icahn Capital's three nominees to the Illumina board instead of the board's chair. This is one of the first proxy contests to go to a vote under the SEC's new universal proxy rules that make it easier for shareholders to mix and match between company and activist board candidates, which may have helped Icahn secure one board seat. Despite securing re-election to the Illumina board at the annual meeting, Illumina's CEO resigned in June 2023.

ii Salesforce/ValueAct, Elliott and others

In January 2023, Elliott reported that it had taken a stake in business software provider Salesforce, Inc and disclosed that it looked forward to working constructively with Salesforce to realise its value. Elliott's arrival at Salesforce came following an announcement by Salesforce that it was laying off 10 per cent of its workforce, citing a challenging operating environment, and after activists Starboard Value, ValueAct Capital and Inclusive Capital had already taken stakes in the company. On 27 January 2023, Salesforce disclosed that it had appointed Mason Morfit and two other independent directors to its board. In February 2023, it was disclosed that activist investor Third Point had also taken a stake in Salesforce. In early March 2023, Elliott nominated director candidates to Salesforce's board. However,

19 id., at pp. 20 and 21.

20 The campaign detail included in this section was generally sourced from public filings.

following Salesforce's announcement of strong fourth quarter and full year 2023 earnings results and a new multi-year profitable growth framework, Salesforce and Elliott issued a joint statement disclosing that Elliott had since withdrawn its director nominations. The 'swarm' of activists at Salesforce is one of many recent situations in which multiple activists (sometimes with different objectives) have targeted the same company around the same time as a means to apply additional pressure.

V REGULATORY DEVELOPMENTS

The US corporate regulatory and governance landscape is constantly undergoing reform. In the past few years, several governmental entities have also demonstrated an appetite for enforcing their existing regulations against activists.

In February 2022, the SEC proposed amended regulations relating to its beneficial ownership rules that may have significant implications for shareholder activism if adopted. The SEC is proposing to shorten the deadline for initial Schedule 13D filings to five days (from 10 days) and to include cash-settled derivative securities held with a control purpose in the beneficial ownership calculation. This change is likely to cause activists to cross the 5 per cent disclosure threshold sooner and to limit the number of securities that an activist could acquire at lower, pre-disclosure prices. The amendments would also increase the scenarios in which two or more persons are deemed to have formed a 'group' under the rules.[21] In April 2023, the SEC reopened the comment period for this proposal through June 2023.[22]

The SEC's new rules mandating universal proxy cards in contested director elections took effect in September 2022. The new rules require companies and activists to use proxy cards that list the names of all director nominees, allowing shareholders to select among nominees in a manner designed to more closely mirror in-person voting practices. In addition, the new rules require activists to solicit holders of a minimum of 67 per cent of the voting power of shares entitled to vote in the election. The 2023 proxy season is key in observing the impact of these new rules, including on both the number and outcome of proxy contests.[23]

The US Department of Justice recently brought several enforcement actions that demonstrate increased scrutiny of interlocking directorships, or simultaneous service on the board of two competitors. This renewed antitrust focus has enhanced the importance of assessing potential competition issues when reviewing future activist nominees.[24]

21 For further information, refer to the Sullivan & Cromwell LLP publication 'Potential Implications of SEC's Proposed 13D-G Amendments', dated 14 February 2022, available at https://www.sullcrom.com/ files/upload/sc-publication-potential-implications-of-sec's-proposed -changes-to-beneficial-ownership- reporting.pdf.

22 US Securities and Exchange Commission press release, 'SEC Reopens Comment Period for Proposed Rule Amendments to Modernize Beneficial Ownership Reporting', dated 28 April 2023.

23 For further information, refer to the Sullivan & Cromwell LLP publication 'SEC Mandates Universal Proxy Cards in Contested Director Elections', dated 18 November 2021, available at https://www.sullcrom.com/files/upload/sc-publication-SEC-mandates-universal-proxy-cards-in-contested-director-elections.pdf.

24 S&C 2022 *Shareholder Activism Review*, at p. 22.

VI OUTLOOK

Shareholder activism will continue to play a significant role in the US corporate landscape. Although company management generally had a stronger record of defeating activists in 2022 as compared with prior years, the SEC's new universal proxy rule and other regulatory and market changes are having an impact on these trends. Going forward, the heightened focus on corporate governance and ESP issues is expected to continue. It is important to remain alert to developments in shareholder activism as the types of activists, companies targeted by activism and activist campaigns evolve.