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WHY WE BOTHER:

A PRIMER IN HOW ACTIVISM ENHANCES RETURNS*

*Jon Lukomnik***

I. INTRODUCTION

I think that Professor Katsoris is right,[1] although I would just urge you to remember that all of the things which get press and publicity get it exactly because there is controversy. Most of the time, Corporate America works well. It is still the world's greatest capital market, it is still a great wealth generator, and, if anything, the public battles are the exceptions that craft the great middle by being outliers. So we should remember that.

I agree with Professor Katsoris that any attempt to have a canned, prescriptive, normative view of this is doomed to failure. Therefore, I intend to avoid doing so by simply telling you why we care at all.

A. The Deadhand Pill

Let me start by telling you a true story about the last time I spoke on this subject just a few weeks ago at the Practicing Law Institute[2] - I always find it interesting that lawyers invite non-lawyers to speak. I was listening to the presentation directly prior to mine about the ongoing Conrail/CSX/Norfolk Southern situation,[3] specifically, the legality of "deadhand pills."[4] This is a great business. We have "white knights,"[5]

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* This speech was part of a symposium held at Fordham University School of Law on March 13, 1997 entitled **Reshaping Corporate Governance & Shareholder Activism for the 21st Century.**

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[1] Constantine Katsoris, *Introductory Remarks*, 2 FORDHAM FIN. SEC. TAX L.F. 1 (1997).

[2] Jon Lukomnik, *The New York City Board of Education Pension Fund, New York City Employee's Retirement System, New York City Fire Department Pension Fund and New York City Police Department Pension Fund: Statement of Procedures and Policies For Voting Proxies*, CONTESTS FOR CORPORATE CONTROL 1997 (PLI Corporate Law & Practice Course Hanbook Series No. 221 1997) (discussing procedures for voting proxies).

[3] Anna Wilde Mathews, *Conrail, CSX Sue Norfolk Alleging Illegal Interference*, WALL ST. J., Dec. 6, 1996, at B8 (discussing the recent takeover controversy surrounding the three major railroads).

[4] *See* Shawn C. Lese, *Preventing Control from the Grave: A Proposal for Judicial Treatment of Dead Hand Provisions in Poison Pills*, 96 COLUM. L. REV. 2175 (1996) (arguing that dead hand pills, or rights plans, containing "continuing directors" provisions should be found per se invalid).

[5] BLACK'S LAW DICTIONARY 1596 (6th Ed. 1990). White Knight is defined as follows: "a potential acquirer usually sought out by the target of an unfriendly takeover to rescue it from the unwanted bidder's takeover." *Id.*

"greenmail,"[6] and "deadhand pills"[7] - wonderful images.

To me, a deadhand pill sounds like Dr. Kevorkian's favorite medication. Actually it is a corporate defense mechanism. It provides for a normal poison pill transaction which greatly increases the numbers of shares in a way that makes it difficult, if not impossible, for a hostile acquirer to take over a company. What makes a deadhand pill unique, however, is that only those individuals on the board at the time it is put into place can remove it. In other words, even if a bidder can get a majority of shareholders to remove the board, that new board, in theory, would be powerless to remove the mechanism.[8] This is a fairly recent development and lawyers are apparently debating its legality.[9] They have asked some penetrating questions. How could a fiduciary obligation continue to be exercised by people who are no longer fiduciaries? Does the time period for which the deadhand pill extends matter? This is a question that Marty Lipton[10] and I were discussing right before this symposium.

But, to me, all that misses the point. To be honest, I do not know if it's legal - to be brutally honest, I do not care. For it's the corporate equivalent of having Congress declare war, having the American people so overwhelmingly opposed to the war that they vote the "rascals" out, and then being told, "Sorry, the new Congress is unable to stop the war because the ousted scoundrels have bound future Congresses." There is just something wrong about that.

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[6] *Id.* at 702. Greenmail is defined as follows: "payment by target company to buy back shares owned by a potential acquirer at a premium over market. [Where t]he acquirer, in exchange, agrees not to pursue its hostile takeover bod." *Id.*

[7] Daniel A. Neff, *The Impact of State Statutes and Continuing Directors Rights Plans*, 51 U. MIAMI L. REV. 663, 671 (1997). The article defines "dead hand poison pills" as provisions which "prevent the redemption of share purchase rights issued under a rights plan, unless that action is approved by a majority of 'continuing directors.'" *Id.* Lese, *supra* note 4, at 2176 (indicating that "dead hand pills," also known as "continuing directors provision," protect corporations against corporate raiders by limiting the abilities of new directors, but noting that they also limit shareholders' rights).

[8] Neff, *supra* note 7. According to this article, "[n]either courts nor commentators have yet considered in much detail the permissability of continuing directors provisions," also known as dead hand pills, which are invalid under New York law, but are of uncertain legality with regard to Deleware law, where there is no case law. *Id.*

[9] *Id.; see also Revco Plans to Revamp Big B Units*, CHAIN DRUG REV., Nov. 18, 1996, at 1 (noting that Revco D.S. and Big B, Inc. had begun litigation over a poison pill provision put in place by Big B, but that the parties agreed to terminate the litigation after Revco sweetened its takeover bid and Big B's board accepted the offer).

[10] Martin Lipton, *Corporate Governance: Does It Make A Difference?*, 2 FORDHAM FIN. SEC. TAX. L.F. 41 (1997).

I tell that story in the interest of disclosure. I am not a lawyer. My role is not to discuss the latest developments on the legal landscape. I am an investor and what I care about is equity in both senses of the word. In my opinion, deadhand pills fail both those tests. They are inequitable since they both impair my rights and decrease the economic value of my equity stake in the corporation. I will agree that there may be situations in which all prescriptives do not apply, but in general that would be my position.

It may be peculiar to be at a law forum as a nonlawyer, but I think what Kim [Morrow] had in mind was for me to answer the fundamental question: Why do we care? Why has corporate governance become so mainstream in the last dozen years that, as Professor Katsoris said, enhancing shareholder value has become a virtually meaningless mantra, whispered by every CEO, corporate raider, corporate governance activist, the press and anyone else who cares to comment? I think answering that question is a good idea.

II. WHY SHAREHOLDER ACTIVISM?

So, that is the question: Why do investors, who in the aggregate possess more than a trillion dollars, belong to the Council of Institutional Investors? Why do people like Michael Price grace the cover of business week?[11] Why do pension funds, mutual funds and individual investors value corporate governance? The answer is really easy: to make money.

A. History of Corporate Governance

Let me begin by giving you the sixty second version of the twelve-year recent history of corporate governance activism.[12] Corporate governance became an accepted investing tool during the 1980s because of the confluence of several underlying factors. These include: (1) the institutionalization of assets, primarily through mutual funds and pension funds; (2) the explosive equity markets (together they trebled

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[11] Jeahnee Kim, *The Legends' Pick; The Favorite Stocks of Five Famous Investors*, MONEY, Sept. 1997, at 70 (noting that when 200 investment professionals were asked which money managers they most admire, Michael Price, the 46 year old chief executive officer of Franklin Mutual Advisers, was among the top five named); Daniel Kadlec, *Going to Bat Against ITT; Two Heavy Hitters Play Hardball. Is This Fair?*, TIME, Aug. 25, 1997, at 59 (discussing Michael Price, who controls $26 billion at Franklin Mutual Advisers).

[12] *See generally* ROBERT A.G. MONKS AND NELL MINOW, CORPORATE GOVERNANCE (1995) (presenting a complete history of corporate governance); *see also* MARGARET M. BLAIR, OWNERSHIP AND CONTROL: RETHINKING CORPORATE GOVERNANCE FOR THE TWENTY-FIRST CENTURY 17 (1995) (providing a primer on corporate governance); GREGORY V. VARALLO AND DANIEL A. DREISBACH, FUNDAMENTALS OF CORPORATE GOVERNANCE: A GUIDE FOR DIRECTORS AND CORPORATE COUNSEL (1996) (reviewing corporate governance from a corporation's perspective, providing a guide for how to act).

institutional assets under management); (3) the rise of modern portfolio theory; (4) the resulting use of indexation,[13] or the replication of an index like the S&P 500, as a way of investing; and (5) at the time - remember, we are talking the late 1980s - the explosion of corporate raiders and M&A activity funded by the popularization of the low investment grade bonds (popularly known as junk bonds). As I warned you, that was the quick version of a very complex history.

B. Institutional Investors

So, what happened? When institutional investors began to perceive that they were being treated less favorably than greenmailers and raiders, who sought pieces of the market pie disproportionate to their capital at risk, the institutional investors had the size and sophistication to fight back without selling out. Because of modern portfolio theory, which I will explain next, the traditional remedy of selling out was not viable.[14]

C. Modern Portfolio Theory

The question somebody always asks is: "Well, if you do not like what is going on, why don't you just sell the company?" Leaving aside the socialist economic answer to that question - that the owner should walk away when the managers do not perform - there is a basic portfolio theory reason why it does not work.

Basically, we invest in stocks as an asset class.[15] Therefore, we want our stocks to replicate that index. If we sell, we lose our ability to replicate the index. If, for example, we were to sell the bottom quartile of an index, we would always be buying and selling because it keeps changing. In this scenario,

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[13] Gretchen Morgenson, *What the Sales Brochure Didn't Tell You*, FORBES, Apr. 7, 1997 at 90 (noting that indexing is rising in popularity and an estimated 8% of the entire U.S. stock market's capitalization is indexed today); *see also* Arlene M. Rockefeller and Anne B. Eisenberg, *The Evolution of Equity Indexation in the U.S. Market*, EQUITY STYLE MANAGEMENT 251 (Robert A. Klein and Jess Lederman eds., 1995) (discussing integration of indexing into equity investment strategies).

[14] *See generally* Geoffrey P. Miller, *The Culture of Capital: Comments on Conley & O'Barr*, 71 N.C. L. REV. 501, 502, 507 (inferring that a conflict exists between the selling out approach to investment where securities are sold if the holder does not agree with the business' actions and the portfolio theory of investment where investors choose sufficiently different stocks and do not concern themselves with extraneous factors).

[15] THE SEC SPEAKS IN 1997 549 (PLI Corporate Law and Practice Course Hanbook Series No. B4-7162 1997) (noting that an asset class is simply a large category of assets, *e.g.*, cash, domestic equities, international equities, bonds).

you wind up with an active portfolio rather than a replication of the index. Therefore, taking the "Wall Street walk,"[16] selling out, is not viable. It engenders huge transaction costs and, more importantly, ruins your ability to track an index.

D. Basic Organization Theory of Exit vs. Voice

With the exit option negated, these rapidly growing and sophisticated institutional investors began trying to reform what they viewed as anti-shareholder policies by using voice.[17] In this case, we used voice in the form of the power of the proxy vote, a series of shareholder resolutions, and publicity to realign the interests of directors and management with owners. In other words, activism began as a defensive strategy.

That defensive thrust was dominant through the end of the 1980s. It began to change, however in 1990, when the California Public Employees Retirement System ("CalPERS")[18] decided to focus its corporate governance activism on companies which had underperformed their peers in terms of total return to shareholders.[19]

Once performance became a significant factor in targeting companies, it was inevitable that they would start measuring whether activism in fact improves the performance — and it does, according to a myriad of studies.[20]

To cite what may be the best-known study, Stephen Nesbitt of Wilshire Associates examined the total returns of fifty-three companies in which CalPERS intervened from 1987 through 1994 for the five

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[16] Blair, *supra* note 12, at 68 (explaining that according to the "Wall Street Rule," shareholders can easily convey their dissatisfaction with management by selling shares).

[17] *See generally* ALBERT O. HIRSCHMAN, EXIT, VOICE, AND LOYALTY: RESPONSES TO DECLINES IN FIRMS, ORGANIZATIONS AND STATES (1970) (describing voice as a control mechanism employed by shareholders).

[18] Barry Rehfeld, *Low-Cal CalPERS*, INST. INVESTOR, Mar. 1, 1997, at 41 (indicating that with assets of $108 billion, CalPERS hefts significant weight in its investment decisions and with nearly half of its investments in stock, the fund has a strong interest in equity style management and creative corporate governance).

[19] *See* Vineeta Anand, *Fund Encourages "Good" Practices: CalPers Top Corporate Citizens*, PENSIONS & INVESTMENTS, Sept. 30, 1996, at 3 (indicating that CalPERS uses a "carrot and stick" approach to reward companies for strong corporate governance).

[20] *See* Henry L. Tosi, et al., *The Separation of Ownership and Control: Increasing the Responsiveness of Boards of Directors to Shareholder Interests*, 4 U. FLA. J.L. & PUB. POL'Y 39, 40 (1992) (finding that firms controlled by management are less efficient than those guided by equity stakeholders).

years prior to CalPERS' intervention and the five years after.[21] Returns for companies without full five-year records post-intervention were included only for the time available. Nesbitt isolated the non-corporate effects by looking only at the "excess return," in other words, the difference between a corporate-specific total return and the market-specific total return over that period. What he found was astounding: the excess return for all companies was negative 75.2% compared to the index in the period before receiving the shareholder proposal, but positive 54.4% in the five years after.

III. INCREASING PERFORMANCE THROUGH ALPHA STRATEGY

Portfolio managers will kill for 1% of the out-performance. We have all heard all the ads, "Looking for your money in mutual funds?" If we assume a 10% stock market return, a 129.6% swing translates to roughly 13% of the out-performance. That is not just phenomenal, it is other-worldly.

The most recent study I have seen, which just came out in the last quarter of 1996, was by McKinsey Consultants. McKinsey looked at it from a different point of view: Does good corporate governance increase the amount that an investor will pay for a company? Or, to put it in the inverse: does good corporate governance reduce the cost of capital for a company? The answer again is yes, by an average of 11%.[22]

Let us put that in perspective. McKinsey noted that for a typical corporation with $1 billion in sales, that would be the equivalent of increasing sales by $110 million forever or decreasing Selling, General and Administrative expenses by 4% forever.[23] Those are very impressive numbers.

These findings are the rationale for what recently may be the most fundamental and least noticed change in corporate governance activism. It has gone from being a defensive strategy that existed in the late 1980s[24] to what investors call an "alpha" strategy, a way to add value above the market without

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[21] *See* Stephen L. Nesbitt, THE CALPERS EFFECT: A CORPORATE GOVERNANCE UPDATE (1995) (finding a significant correlation between shareholder involvement and corporate wealth generation).

[22] Jennifer Van Heeckeren, *Managers' Journal; Why Investors Push for Strong Corporate Boards*, ASIAN WALL ST. J., June 30, 1997, at A14 (noting the McKinsey Study which found that money managers looking for long term value were willing to pay higher prices for companies with good independent boards).

[23] *Id.* (noting that 50 money managers said they would pay an eleven percent premium for good governance).

[24] *See* Rehfeld, *supra* note 18, at 41 (noting that corporate governance was born as a reaction to greenmail).

engendering additional systemic or market risk.[25] It is not leveraged, it is not in a different market, you are just specifically focusing on those corporations.

A. The Alpha Strategy in Practice

The added value of the alpha derives from two complementary aspects of the strategy: security selection and implementation.[26] Although sequential in execution, the two are tightly intertwined.[27]

The selection of focus or target companies is designed to discover undervalued corporations.[28] While similar to traditional contrarian or value investing, it differs in that corporate governance activists add selection screens which focus on the ability to force the market to recognize the value ahead in focus companies. Everybody has a buy price — "I am going to buy it at this, I am going to sell it at that." Corporate governance activists try to decrease the time between when the market realizes it, between your buy and sell price, so that the market focuses on that increment and gets the multiple expansion done quickly.[29]

In keeping one eye on the unique implementation part of activism, not just on the unrecognized value, we look for companies with the ability to get the market or themselves to recognize the value inherent in the company. At the very least, we look for companies which have few barriers to recognizing the value in having few conflicted directors and few related transactions that might have other motivations.

Now, to understand why, let us just suppose for analysis that both companies A and B own money-losing subsidiaries outside the parent company's core business, and that both sell for what would be a 20% discount to the market multiple they would command without that unrelated subsidiary. Further assume that A and B are identical except for ownership structure. Company A is largely owned by external

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[25] Jon Lukomnik, *Shareholder Activism: Two Alpha-Generating Strategies In One*, ALPHA: THE POSITIVE SIDE OF RISK 31 (1996) (discussing shareholder activism as value added strategy and a deviation from expectation which cannot be managed).

[26] *See* Ronald A. Sages and H. Michael Kedan, *Supercharging Popular Wealth Transfer Planning Vehicle*, TRUSTS & ESTATES, Aug. 1, 1996 (discussing securities selection and implementation in alpha strategy).

[27] *Id.*

[28] *See* Nesbitt, *supra* note 21.

[29] *See* Marvin L. Damsma and Gregory T. Williamson, *Managing Risk in the Aggregate Portfolio: The Reward of Portable Alpha*, ALPHA: THE POSITIVE SIDE OF RISK 16 (1996) (discussing the reevaluation of traditional operating structures by using alpha and risk management strategies to achieve desired return goals).

institutions and has a new CEO who inherited the problematic subsidiary, whereas Company B is owned by a hodgepodge of individuals and institutions with the largest minority stake held by the long-time CEO's family trust.

Which corporate management do you think would act more quickly to erase that market discount and thereby reward shareholders? While both companies may ultimately divest themselves of the subsidiaries, most investors would believe that Company A would act more quickly. If it does not act, Company A would be more susceptible to outside pressure from either corporate governance activists or corporate raiders than Company B.

Although the above scenario is admittedly a bit stark, it illustrates the point. The total potential multiple expansion in both situations is the same, but the ease of achieving that expansion and time necessary to achieve it differs.[30] Since investment returns are time weighted, this can have a profound effect.

New York City, for example, uses eight quantitative and qualitative selection criteria. The first and most important factor is to screen total return of all our holdings against industry-specific averages for one-, three-, and five-year periods. The three screens the New York City funds use to judge the susceptibility of the company to change include: (1) Institutional ownership — the higher the institutional ownership, the more likely a change agent can be successful; (2) Corporate governance structures; and (3) How the company is perceived by the investing public and the business press.[31] This factor has an inverse correlation: the worse the public perception of a company, the more susceptible it is to pressure to change. The New York City funds also perform fundamental analysis designed to rule out companies which only appear to be improving and to determine the relevance of extraordinary items, such as write-downs for reorganizations.[32]

What we have discovered, along with other institutional investors is that if the targeting is good enough, we do not always have to be the agent of change. For example, during the past few years we

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[30] *Id.*

[31] *See generally* Lukomnik, *supra* note 2 (discussing New York City Employees Retirement System ("NYCERS") policies and proxy voting procedures).

[32] *See* Alyssa A. Lappen, *BGI Thinks Big*, INST. INVESTOR, Apr. 1, 1997, at 62 (discussing the analytical strategy of outperforming the S & P in a very risk-controlled manner).

targeted both Maxxus[33] and American Cyanamid,[34] and within a few months they were both acquired. We also targeted Charming Shoppes, a troubled fashion retailer, which includes Fashion Bug, and we are pleased to say that the board of directors was on top of the situation, replaced the CEO, and turned around the company.[35]

Clearly, these combined processes of focusing on discovering undervalued corporations together with examining their susceptibility to change have been validated by both the market's merger and takeover specialists and enlightened boards of directors who take their obligations seriously. Other investors have discovered the same to be true - that performing the selection analysis with an eye towards future intervention, ironically, often means that intervention is not necessary.

Greenway Partners, a New York-based private money management company, has managed approximately $200 million in this contrarian corporate governance style since 1993.[36] Greenway's two partners, Gary Duberstein and Alfred Kingsley, are willing to intervene publicly and confrontationally, if necessary, as they did at U.S. Shoe and Woolworth, but they have no desire to do so unless necessary.[37]

Greenway Partners has also found that managements themselves by their actions, or the market through merger and acquisition activity, force recognition of underlying value. They stated something to the effect of: when stocks go up by themselves, we are of course happy to remain quietly on the sidelines. In that category are companies such as IBM, Marion Merrell Dow, and Seagrams. When they do not, as

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[33] Enrique P. Sanchez, *Capital Flows into Latin America: Stronger Than Ever*, BUS. ECON., July 1, 1996 (discussing the purchase of U.S. based Maxxus by YPF, a former Argentinian state-owned oil company).

[34] *See* J.G. Delinassios, *Merger Mania—Faith or Folly?*, IN VIVO BUS. & MED. REP., Sept. 1, 1996, at 1 (discussing the hostile takeover of American Cyanamid).

[35] *See Charming Shoppes Inc.: Retailer Swings to a Profit But Falls Short of Estimates*, WALL ST. J., Mar. 12, 1997, at B4 (discussing Charmings' net income after a recent restructuring).

[36] Dan Dorfman, *Tisch Sees Beauty in Ugly Bethlehem Steel*, FIN. WORLD, Feb. 18, 1997, at 14 (calling Al Kingsley of Greenway Partners an "activist money manager"); Judy Temes, *CEO's Time Runs Low to Restore Woolworth; Crumbling Business, Spin-Off Push May Foil Farah's Three-Year Plan*, CRAIN'S N.Y. BUS., Feb. 12, 1996, at 3 (noting that Al Kingsley is the senior managing director of Greenway Partners L.P., a Manhattan-based firm that is Woolworth's single largest shareholder); *see also Proxy Season Reveals Trend Toward Spinoff Proposals*, CORP. FINANCING WEEK, July 8, 1996, at 4 (noting Kingsley of Greenway participation in a proxy to Unisys to change the company's structure and his belief that "corporate management rarely warms to shareholder suggestions on strategy").

[37] Riva Atlas, *Unisys Watch*, FORBES, Sept. 3, 1996, at 236 (discussing Al Kingsley and Greenway Partners' dealings with Unisys and Woolworth).

was the case with U.S. Shoe, we are prepared to take action.[38]

IV. Shareholder Activism Tipping the Balance of Power

Action is, of course, the major difference between corporate governance investing and traditional investing techniques.[39] So that is the security selection. What is the action? What can we do?

The step following security selection is to decide whether and when to approach management. While some successful investors wait for some time after identifying the focus company, others, particularly large institutional investors like us who have held the security for some time, usually in an index fund, tend to approach the company soon after selection. Virtually everyone begins by politely and formally writing or calling the company to request a meeting with top management.

The discussion at that meeting, which is often salutary, and therefore never becomes public, has evolved into the key point of the entire process. The nature of the discussion varies from investor to investor. We tend to hold initial two-hour meetings with top management, usually with the CEO, General Counsel, and sometimes the CFO or COO, which break down into three distinct parts:

(1) a recap of the typical investor relations program, similar to what the company presents to Wall Street;

(2) a longer term overview which stresses the heart of the discussion of the strategic plan of the company and what the corporate governance of the company does, what the directors actually do, how they have input it into the strategic plan, how they benchmark the strategic plan; and

(3) finally, any proposed reforms.

As long-term passive investors, we do not pretend to know a lot about each individual company. I notice the question "Are There Too Many Cooks in the Corporate Kitchen?" is the focus for the panel

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[38] *See generally* ROBERT S. REDER AND PHILLIP BERKOWITZ, RECENT DEVELOPMENTS IN PROXY CONTEST (PLI Corporate Law and Practice Handbook Series No. B4-7114 1996) (generally reviewing Greenway's activities and philosophies).

[39] *See* Frank H. Easterbrook and Daniel R. Fischel, THE ECONOMIC STRUCTURE OF CORPORATE LAW 196-7 (1991) (suggesting that shareholder actions in corporate control generate gains for shareholders and the corporation).

discussion. I would say that we don't even go near the kitchen. We are very content to be in the dining room asking whether the chef knows what he is cooking, as opposed to cooking ourselves.

What we look at are whether the corporate mechanisms are in place and working. What Dale Hanson once said is: "Are the lights on? Is anyone home?" [40]

We ask about the independence of the board, the skill sets of the board, the nature of the incentive compensation plans for both management and the board, the interaction of boards and their management teams and particularly the strategic planning. What we really try to do is to remove any impediments to good corporate governance, not dictate what corporate strategy should be. [41]

Dialogue often has a salutary effect on the board for a not-immediately-apparent reason. Some years ago, efficiency experts at the Hawthorne factory in Chicago, experimented with different lighting and other environmental changes in an effort to improve productivity. They turned up the lights and productivity went up, they turned down the lights and productivity went up, and they stretched the tables and productivity went up. What they found was that when they took all the changes away and went back to the pre-experimentation state, productivity went up. Behavioral scientists christened this the Hawthorne Effect, explaining that people tend to perform better when they know someone is watching what they do — a revolutionary idea.[42]

A corporate governance activist, Nell Minow of the Washington, D.C. based Lens Fund puts it a different way, only partially tongue in cheek. "Board members," she says, "are like subatomic particles. They act differently when observed."[43]

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[40] Rehfeld, *supra* note 18, at 41 (discussing the evolving corporate governance philosophy at CalPERS and noting that Dale Hanson was the CEO of CalPERS until 1994, when he was replaced by the current CEO, James Burton).

[41] *See* Carol B. Swanson, *Corporate Governance: Sliding Seamlessly into the Twenty-First Century*, 21 J. Corp. L. 417 (1996) (addressing the difficulty of aligning the interests of shareholders and management).

[42] Peter Wilby, *Blunkett's Plans for Raising Performance in Schools Will Fail Unless Some Gaping Holes in Them Are Filled. The Fillings Will Not Be Popular. (U.K. Secretary of Education, David Blunkett)*, NEW STATESMAN, July 11, 1997, at 13 (noting that the "Hawthorne Effect" is that peoples' activities change when their environment changes or when they are being watched; tracing the effect back to its origins in a Chicago plant owned by Western Electric in the 1920s).

[43] Casey Bakro, *This Minow Views Ailing Firms with Cold Eyes Pressured by Hei Lens Group, Some Companies Whose Stock Was Underperforming Have Replaced Chief Executives and Restructured - Sometimes Laid Off Employees*, CHI. TRIB., Nov. 10, 1996, at 1 (Giving Nell Minow's background as well as quotes).

The point is that sometimes we just have to let people know that someone is watching. That is what we do. There are those, such as Greenway or, more recently, Guy Weiser Pratt,[44] which is currently at battle with Rexine — who rely on fundamental research and strategic insight to suggest specific structural or personnel change.

For instance, in the scenario with Company A and B discussed earlier,[45] we would usually be happy to know that the board was seriously considering what to do with that subsidiary, that they had good information and that they were taking their obligation seriously.

Another type of corporate governance activist, which the proxy community has now labeled as "destabilizers," as opposed to corporate raiders, might come with a specific point to the table of not only getting rid of the subsidiary, but also addressing who you should sell it to and what the tax consequences might be.[46] If discussion does not work, there are a whole host of other things we can do:[47]

- there are proxy resolutions that get filed, which are the subject of much debate and dispute;[48]
- there are "just vote no" campaigns[49] (for example, we voted against the directors at Disney, for example, over Michael Ovitz's and Mike Eisner's compensation package);[50]

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[44] Jill Dutt, *Arbitrageurs Who Didn't Bail Out Winning the Office 'Poker Game'*, WASH. POST, Mar. 13, 1997 (citing Guy Wyser-Pratt, President of Wyser-Pratte & Co. Inc., as one of Wall Street's "best-known arbitrageurs"); *see also* Linda Kay Sakelaris, *Investors Launch Proxy Fight Against Bethesda Satellite Co.*, RADIO COMM. REP., Apr. 14, 1997, at 27 (discussing Guy Wyser-Pratte and his company, noting their ownership of 2.56 percent of Comsat).

[45] *See supra* pp. 11-12.

[46] *See* Nell Minow, *Proxy Reform: The Case for Increased Shareholder Communication*, 17 J. CORP. L. 149 (1991) (discussing the balance of shareholder powers through an active voice).

[47] John Pound, *Beyond Takeovers: Politics Comes to Corporate Control*, HARV. BUS. REV. 83-93 (Mar.-Apr. 1992) (discussing a wide range of formal and informal governance roles ranging from shareholder/director meetings, special committees, and director nominations to more aggressive tactics such as media campaigns and high pressure contacts).

[48] Jonathan L. Johnson, Catherine M. Daily and Alan E. Ellstrand, *Boards of Directors: A Review and Research Agenda*, 22 J. MGMT. 409 (1996) (discussing how the proxy is an important factor in firm management, because major firm decisions are decided by a vote of the shareholders, and when shareholders sign proxy cards allowing management to vote their shares, the separation of ownership and control comes into question).

[49] Joseph A. Grundfest, *Just Vote No: A Minimalist Strategy for Dealing with Barbarians Inside the Gates*, 45 STAN. L. REV. 857 (1992) (summarizing the "just vote no" campaign whereby shareholders identify publicly traded companies which are underperforming and express their lack of confidence by withholding votes for the incumbent board).

[50] *Will Controversy Steal Disney's Show?*, ORLANDO SENTINEL, Feb. 23, 1997, at H1 (noting that institutional investors voted against Eisner's compensation package, and protested Ovitz's payout by withholding votes for five Disney board members who were up for re-election.); *see also* Linda J. Barris, *The Overcompensation Problem: A Collective Approach to Controlling Executive Pay*, 68 IND. L.J. 59, 65 (1992) (citing evidence that executives are being amply rewarded despite less than stellar performance).

- there is publicity; and

- there are lawsuits, something we've never done, but certainly not unknown to the members of this audience.

But I promised I would limit this to a reasonable amount of time, and I suspect that is exactly what Jamie is going to talk about, which is what is out there on the horizon and what people are doing this year. I see you choking. Did I get that wrong?

MR. HEARD: Close enough.

MR. LUKOMNIK: So this is probably a good place to stop because there are a lot of other people, I think, who can give you a perspective on what the legal mechanisms are to achieve corporate governance change.

What I wanted to leave you with was the philosophical overview of why we would bother doing it at all. I want to thank the *Fordham Finance, Securities and Tax Law Forum* and Kim Morrow for this opportunity. Thank you.