

AGENDA

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Defenders Against Activist Attacks Redesign Their Armor

By Lindsay Frost

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Law firms, investment banks and specialist consultants that offer boards protection against activist investors are competing for business by widening the services they offer.

The wave of activist investors continues as more than 200 proxy contests have been announced or completed so far this year, according to FactSet. Experts say that boards need to consider retaining a complete activist defense team to analyze the company and prepare for a potential battle.

Goldman Sachs has picked up the most business this year, according to FactSet. It has been hired to defend companies in 10 proxy contests, including in the high-profile fight at DuPont. In July, the investment bank restructured its activist-defense team to combine it with its other M&A and shareholder practices.

Fellow investment bank Morgan Stanley in April hired David Rosewater, a former partner at Schulte Roth & Zabel, to head its global shareholder activism defense practice. Rosewater previously was commonly employed on the activist side of campaigns.

Banks and law firms are taking their advisory knowledge from M&A deals and hostile shareholder cases and applying it to activist defense.

"We have negotiated agreements with shareholders as long as we have represented companies, but there is a new type of agreement when dealing with activists," says **Steve Stokdyk**, global co-chair of **Latham & Watkins'** public company practice.

Latham & Watkins was hired by Allergan in late 2014 to defend the company against an aggressive takeover bid by Pershing Square-backed Valeant. Latham & Watkins — which has been the busiest law firm involved in activist defense this year, handling seven campaigns — has increased its focus on bylaw provisions for dealing with activists, Stokdyk says.

The FactSet data shows that, in 224 activist campaigns announced in 2015, companies have employed 35 different law firms and banks as activist advisors.

Defense Packages

Typically, companies hire law firms, banks, PR firms, proxy solicitors and other consultancy services as a complete package, as each company has different services to offer.

"There's a lot of parties involved — the board, management, law firm, investment bankers, a PR firm, a proxy solicitor — six to seven parties, which all need to be managed and coordinated," Stokdyk says.

The two biggest issues boards come to law firms for typically are boardroom analysis and advice for possible M&A transactions that are proposed by activists, Stokdyk says.

"Activists will propose [that] new directors [be] added to the board, which raises issues in terms of appropriateness, board dynamics and practical issues with removing an existing director," Stokdyk says. "The

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second key [issue] is when a specific action is proposed at the company, like divesting a particular division, we help boards analyze to determine if that's an appropriate action for the company."

Public relations and communication is an important defense tool that often gets overlooked, says Steve Balet, managing director of FTI Consulting's strategic communications practice, which specializes in activism. Balet says communicating with employees, suppliers and customers is one aspect FTI helps boards shape the message in case an activist fight is playing out through the media and there are mixed signals.

"If a well-known activist wants you to sell or split a business or return shares, you have to explain to employees why it's a valid option or not, to make sure you contain the situation at home and there's no destruction through your employee base's negative mood or message," Balet says.

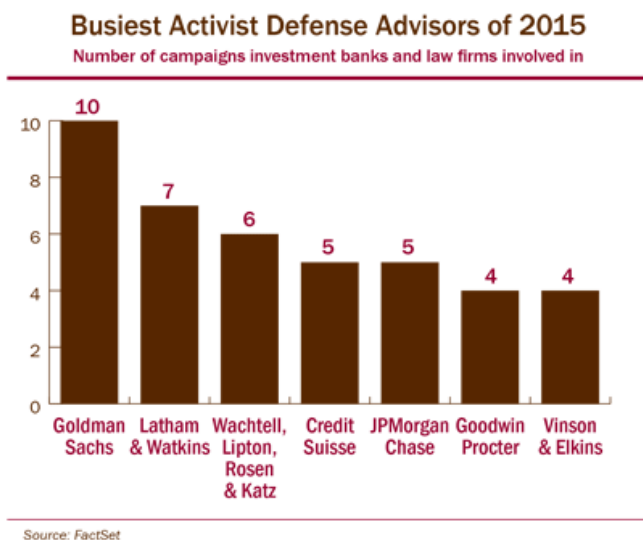
Communication with shareholders is one discipline that has changed in defending against activists, Balet says. Boards are encouraged to contact their shareholders through surveys, meetings and improved investor relations programs.

However, digging through financial statements, stock performance, operational issues and balance sheets are also important steps in setting up a defense. John Houston, head of Fredrikson & Byron's public company practice, says that banks tend to offer pre-packaged defense programs that analyze company structure and performance metrics.

"Morgan Stanley's activism defense team offers differentiated advice based on a thorough understanding of the activism environment, key players, critical trends, industry dynamics and sources of capital, as well as best-in-class execution services for any resulting corporate actions," Rosewater writes in an e-mail.

Banks typically have fixed fees for these services, Houston says. They make a pitch of what they can offer, do a quick assessment of what the company needs, and charge accordingly. Law firms may charge extra fees for activist defense services depending on variables such as if the proxy fight is in the public domain, it has a shorter time frame and there is a need to scrutinize more areas.

"Alternative fee arrangements from law firms are not uncommon," Houston says. "Most of what we charge is by the hour with our standard rates and good advice. But, since our clients [in these situations] need to be more efficient and we are offering more discreet advice in the intense heat of a battle and could be working all night with all hands on deck, there may be higher fees."



Houston says there is an "art" to this type of legal defense and each defense strategy is considered on a case-by-case basis. He says he recently dealt with a client that was targeted by an activist, which became combative and public. The board determined it was best not to fight after assessing its "appetite to resist" and alternatives. The board decided to put the activist nominee to a shareholder vote.

"There are a lot of successful negotiations with activists, and sometimes it's a good thing to have an activist on the board," says John Stout, chair of the committee on corporate governance, business law

section, of the American Bar Association. "You really have to think about it on an individual basis."

Premeditative Preparation

Providers of these services say preemptive in-depth evaluations are the best way to avoid an unwanted activist approach.

“As preemptive preparation, Morgan Stanley will assist the board of directors and senior management of a company with vulnerability, strategic and shareholder analysis, as well as execute a timely and effective engagement with and response to an activist if one materializes,” Rosewater writes.

Balet says that the preemptive side of activism defense services is growing steadily as companies realize how important it is to be prepared. Firms will provide evaluations of key areas activists typically look at before they file a 13-D.

Experts say that a company that is able to analyze itself ahead of time is one which could be more successful in case of a proxy fight with an activist.

“You can help a company by asking them the kinds of questions an activist would so they can do the research themselves. [Law firms] are quite often in a position of encouraging a company to do some self-analysis and weakness analysis,” Stout says.

Above all, boards that study investor news, market trends, M&A deals and potential deals, and shareholder voting patterns will remain ahead of the pack, says Dave Wilson former CEO and current director at CoreSite Realty Corporation. Wilson says he has experience of being on a successful activist board slate and has also seen companies “dig in their heels” and lose proxy fights due to lack of knowledge and defense.

“My best defense is having the board look at the company with eyes wide open and asking itself questions that an activist would ask and being prepared to embrace change, like a merger, while being aware of what the impact would be,” Wilson says.

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