Shareholder Activism & Engagement 2019

Contributing editors
Willem Calkoen and Stefan Wissing

LEXOLOGY
Getting The Deal Through

Publisher
Tom Barnes
tom.barnes@lbresearch.com

Subscriptions
Claire Bagnall
claire.bagnall@lbresearch.com

Senior business development managers
Adam Sargent
adam.sargent@gettingthedealthrough.com

Dan White
dan.white@gettingthedealthrough.com

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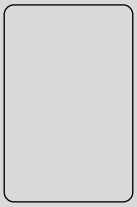

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Lexology Getting The Deal Through is delighted to publish the fourth edition of *Shareholder Activism & Engagement*, which is available in print and online at www.lexology.com/gtdt.

Lexology Getting The Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Lexology Getting The Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on Brazil, Hong Kong, Israel and New Zealand.

Lexology Getting The Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.lexology.com/gtdt.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Lexology Getting The Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, Willem Calkoen and Stefan Wissing of NautaDutilh, for their continued assistance with this volume.

London
April 2019

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Introduction

Willem Calkoen and Stefan Wissing
NautaDutilh

In 2018, shareholder activism was on the rise again: the number of new campaigns and companies publicly targeted reached a reported record high and activist assets under management remained at elevated levels.

While seasoned activist funds continue to be responsible for most of the high-profile activist campaigns, the number of new firms entering the activist space grew by almost 75 per cent, reflecting the continued expansion of activism as a tactic. Elliott Management stands out as it continued to be the most prolific and, in many cases, aggressive activist in 2018, publicly targeting 22 companies and having the largest market value of current activist positions (as reported by Lazard).

Against the backdrop of a robust M&A market during most of 2018, M&A-related activism was prevalent and ranged from instigating deal activity by pressing for splits, spins and sales (sometimes to the activist itself) to activists intervening in announced transactions by pushing for a price increase (bumpitrage). Elliott Management's embrace of private equity strategies (eg, the buyout of Athenahealth) and transactions such as Starboard Value's investment of up to US$250 million in Papa John's through a PIPE transaction, fit a trend where the line between activism and private equity becomes increasingly blurred.

A record number of board seats was won by activists in 2018, both within and outside the US mostly through negotiated settlements rather than protracted public campaigns culminating in a shareholder vote. In many cases, settlements involved adding new independent directors with public company director experience rather than adding activist employees. The addition of 'activist-minded' directors to a board has an ongoing impact on companies after a campaign, as it changes the dynamics within the board and may cause changes in a company's strategy that may culminate in M&A activity.

The stockmarket declines around the globe in the fourth quarter of 2018, offered activists attractive entry points for new positions while at the same time benefiting short activists. US debt markets showed a rise in default activism, where activists amass a large short position in corporate debt and then use a much smaller long position to assert that the company is in default on its corporate debt so that they can reap gains on their (net) short position (see Wachtell Lipton's memo titled *The Rise of the Net-Short Debt Activist*).

Hedge fund activism and its economic consequences continued to be widely debated. A 2018 research paper by Ed deHaan, David Larcker and Charles McClure titled *Long-Term Economic Consequences of Hedge Fund Activist Interventions* found that 'on a value-weighted basis, which best gauges effects on shareholder wealth and the economy . . . pre-to-post activism long-term returns are insignificantly different from zero'.

No company is immune to shareholder activism

Neither location or industry sector nor market cap or brand recognition make a company immune to shareholder activism.

While the majority of public campaigns and capital deployed is still targeting US companies, campaign activity increasingly has a global reach. Campaign activity in Europe and Asia-Pacific remained high compared with 2013 to 2016. US activists, led by Elliott Management with a record 13 European campaigns initiated in 2018, accounted for many of the activist campaigns outside the US.

As in previous years, activist campaigns targeted companies in a range of industries. While some individual managers target companies in specific sectors, activist investors as a whole do not display any clear preference for any particular sector (with many activist funds remaining industry generalists).

The top five sectors in terms of capital deployment and number of companies targeted in new campaigns were technology, industry, consumer, financial institutions, and infrastructure (including energy). Activists remain focused more on characteristics such as undervaluation based on corporate fundamentals, lagging stock performance relative to the market generally, low leverage or strong cash positions and announced or potential M&A than the industry in which the company operates.

The list of companies targeted by activist campaigns in 2018, or in which activists acquired a significant stake, spans a variety of sectors and includes large-cap companies and national champions such as Allergan, Altaba, Barclays, Bayer, BT Group, Campbell's, Cigna, Citigroup, Deutsche Bank, eBay, Hyundai, Lowe's, Nordea, Papa John's, Pernod Ricard, PPG Industries, Sempra Energy, Sky, Thyssenkrupp, Telecom Italia, Toshiba, 21st Century Fox, Unilever, United Technologies and VMware.

Pure play activist hedge funds seeking to enhance corporate governance/ESG profile

With the vocal emphasis by the large passive index funds (BlackRock, State Street and Vanguard) on corporate purpose, environmental, social and governance (ESG) and long-term value creation, the rise of ESG-oriented activism by pension funds and other institutional investors, and to counter criticism that activists are too short-term focused, activist hedge funds are seeking to enhance their corporate governance and ESG profile.

For instance, at Elliott Management, Paul Singer's 2017 commentary in the *Wall Street Journal* titled 'Efficient Markets Need Guys Like Me', in which he argued, among other things, that activists and index funds are natural allies, was followed up in 2018 by a newly created head of investment stewardship position aimed at cultivating better relations with index funds and other major institutional investors and enhancing Elliott's profile by incorporating investors' corporate governance priorities into the company's campaigns.

Pure play activist hedge funds such as Trian Fund Management, ValueAct Capital and Elliott Management increasingly become members of, and attend conferences organised by, governance-focused organisations such as the International Corporate Governance Network and the Council of Institutional Investors.

JANA Partners announced plans to launch an impact investing fund, the JANA Impact Capital fund, which will focus more on ESG factors and social activism and is expected to formally launch this

year. Ahead of the formal launch, JANA Partners already teamed up with CalSTRS in pushing Apple to develop new tools and provide insights to help parents address the overuse of Apple devices among young people.

Outlook

Shareholder activism is expected to persist in 2019. Key trends that are likely to continue are:

- a continued growth of the relative rate of activism outside the US, as activist hedge funds seek attractive opportunities across the globe;
- pension funds and other institutional investors remaining vocal on environmental, social and (corporate) governance issues in the broadest sense, including diversity, board refreshment, environment, sustainability and climate change;
- an increased embracing of diversity and ESG issues by, and integration of such ESG themes into campaigns of, traditional activist hedge funds; and
- growing awareness within boards of the risk of becoming an activist target and the need to ramp up preparedness and effective engagement with major shareholders and other stakeholders.

Each jurisdiction has its own regulations and practices when it comes to shareholder activism and engagement. While the chapters in this book show there is growing convergence in certain areas, important differences remain between countries. We hope the concise jurisdictional overviews offer the reader a helpful first look at key activist-related topics in the various countries, enable convenient comparisons between jurisdictions and give food for thought as reading about the issues, practices and solutions in other countries often offer new insights and understandings relevant to one's own laws and best practices.

We are thankful for having so many recognised thought leaders from around the globe contribute to this essential reference guide. We look forward to following future developments with great interest as the activist landscape continues to evolve.

Austria

Christoph Nauer and Daniel Reiter
bpv Huegel

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The main source of law relating to shareholder activism and engagement is the Austrian Stock Corporation Act (AktG), including the fundamental principle of equal treatment of shareholders (in particular, equal voting, dividend and information rights) (section 47a, AktG) and a limited duty of loyalty of the shareholders with respect to the company's and the other shareholders' legitimate interests. The Austrian Stock Exchange Act and the Austrian Takeover Act provide provisions applying only to companies whose shares are admitted to stock exchange trading on regulated markets (section 3, AktG) and their shareholders.

The provisions governing shareholder actions are part of Austrian federal law, partially (particularly regarding listed companies) based on EU directives and regulations.

Shareholders can enforce their rights generally in front of the Austrian commercial courts. The competence of the Austrian commercial courts is binding and cannot be replaced by, for example, arbitrational proceedings. The management of the company is in general personally liable to the company but not to the shareholders if damage occurs owing to a violation or non-compliance with statutory law or the provisions of the articles of association (AoA). Regulations concerning listed companies are enforced by the competent supervisory body, the Austrian Financial Market Authority (FMA).

The breach of specific obligations of the management can be prosecuted as a statutory offence according to the Austrian Criminal Act, for example, inaccurate or incomplete information with respect to net assets, financial positions or results of operations in certain declarations, reports or disclosures.

Companies of certain sectors (eg, banking and insurance) are subject to additional regulations, compliance with which is supervised and enforced by the FMA or EU institutions.

Apart from statutory provisions, the Austrian Corporate Governance Code (CGK) includes 'comply or explain rules' as well as recommendations. The CGK becomes binding by declaration of commitment. If a company's shares are admitted on a regulated market in the EU or ECC or if companies' securities are admitted on a regulated market and its shares are traded on a multilateral trading facility, declarations on commitment or opt-out (in the latter case including reasoning) to a corporate governance code and comply or explain with respect to the rules of the corporate governance code, are mandatory.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

In Austria, the appearance of shareholder activists and activist campaigns is still a rather new phenomenon. Although the number of active shareholder activists is limited, the number of activist campaigns has increased significantly over the last decade.

The chances of success depend essentially on the shareholder structure of the target company as well as the position of proxy advisers. It is expected that proxy advisers will eventually support the strategies of activist shareholders in Austria, as seen in the proxy fight at Conwert Immobilien Invest SE, where activist shareholders have been supported by proxy advisers. Thus, the candidates proposed by activist shareholders successfully challenged the candidates proposed by the management for the board of directors. Activist shareholders can expect support from other shareholders, provided these can also benefit, and the proposals are reasonable with regard to the company.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

Shareholder activism is not industry-specific. In general, shareholder activism has not played a very significant role in Austria due to the prevalence of listed companies being firmly controlled by one shareholder or a group of shareholders. In recent years in Austria, real estate companies were somehow the focus of shareholder activism. In our view, however, that cannot be linked directly to the industry. Companies targeted by shareholder activist strategies include, for example:

- Flughafen Wien AG (Vienna Airport) (aviation);
- Conwert Immobilien Invest SE (real estate);
- IMMOFINANZ AG (real estate);
- S IMMO AG (real estate);
- C.A.T. oil (oil field exploration);
- BWT AG (water technology); and
- Wienerberger (construction).

4 What are the typical characteristics of shareholder activists in your jurisdiction?

In the rather rare cases in Austria so far, mainly hedge funds have been seen as activist shareholders. However, shareholders of listed companies have started to make more active use of their rights, resulting in higher numbers of opposing votes in the elections of supervisory board members and auditors and rejection of large volume share capital issuance authorities to the management board carrying a right to exclude subscription rights of the shareholders. Activist shareholders must be

discerned from notorious claimants trying to leverage by blocking resolutions on structural measures.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

Activist shareholders in Austria tend to focus strictly on profitability and the valuation of companies. Sociopolitical agendas are mainly the focus of non-government organisations, chambers and other organisations.

Shareholder activists focus specifically on:

- corporate structure, corporate strategy and restructuring measures;
- takeover bids;
- management and supervisory board composition;
- return of value to shareholders (share buy-backs, additional dividend payments);
- divesture, acquisition, merger proposals;
- investigation of management actions by a special auditor; and
- opposing delisting attempts.

In particular, underperformance of the management and – in the case of listed companies – low stock prices (undervaluation) attract shareholder activists.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

Activist shareholders in Austria apply well-known strategies to leverage their influence beyond their proportionate shareholding through informal measures such as issuing open letters to the management and campaigns publicly voicing their dissatisfaction with the management's strategy.

However, shareholders also increasingly take advantage of the possibilities provided to them by corporate law, such as to contest shareholder resolutions in court. However, in general, shareholder activists do not primarily intend to block resolutions in shareholders' meetings by using their minority shareholders' rights. As common practice, the share exchange ratio of mergers and the squeeze-out compensation are examined in court, however, without blocking the transaction as such.

Depending on the approach and the quality of the proposals of activist shareholders, it is expected that the boards of listed companies are interested in a dialogue with activist shareholders making constructive proposals or who can be expected to gain substantial support from other shareholders.

Activist shareholders can also benefit from several legal measures that force companies to engage constructively with them, such as the right to request a shareholders' meeting or the right to include items on the agenda of the shareholders' meeting.

Shareholder minority rights, regardless of the number of shares held, include:

- attending and speaking at shareholders' meetings (sections 111 and 112, AktG);
- exercising voting rights; and
- asking questions and receiving answers at the shareholders' meetings in connection with items on the agenda (section 118, AktG); and the right to challenge a shareholder's resolution in court (sections 196 and 201, AktG).

Shareholders individually or collectively representing 1 per cent of the share capital may:

- submit motions (counter proposals) to agenda items (outlined in question 6); and
- request the review of the amount of consideration for a mandatory offer as well as for a voluntary offer aimed at gaining control with the Austrian Takeover Commission (section 26, paragraph 5 and section 33, paragraph 2, No. 4, Austrian Takeover Act).

Shareholders representing 5 per cent of the share capital may:

- call for a shareholder meeting (section 105, AktG), which can be enforced in court in case of non-compliance;
- request to amend items to the agenda (section 109, AktG);
- request an audit of the annual accounts by a different auditor for good cause (section 270, paragraph 3, Austrian Commercial Code);
- request that certain claims are levied by the company against certain persons or deny a waiver or settlement regarding such claims, in connection with the establishment, post-formation acquisitions and management of the company, if the claims are based on certain reports; and
- call as shareholders of an acquiring company for a shareholder meeting during the course of a simplified merger, up to a month after the transferring company resolved upon the merger, where it is resolved upon if the merger shall be approved (section 231, paragraph 3, AktG).

Shareholders representing 10 per cent of the share capital may:

- file for removal of a supervisory board member for good cause by the court (section 87, paragraph 10 and section 88, paragraph 4, AktG); and
- request that certain claims are levied by the company against certain persons or deny a waiver or settlement regarding such claims, in connection with the establishment, post-formation acquisitions and management of the company.

Shareholders representing 20 per cent of the share capital may:

- deny a waiver or settlement regarding certain claims against members of the management or supervisory board or founding shareholders (section 43, section 84 para 4 and section 99 AktG).

Shareholders representing more than 25 per cent of the share capital present at the shareholders' meeting may (unless the majority requirement is reduced in the AoA):

- veto changes of the company's AoA, including capital measures, selective share-buy backs; and
- veto measures carrying exclusion of subscription rights of the shareholders.

Shareholders representing one-third of the share capital may:

- elect an additional member to the supervisory board in the case that three or more members of the supervisory board are elected in one shareholders' meeting and one candidate got at least one-third of the votes in all prior elections. In this case, that candidate gets the last mandate without a further election.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

At shareholders' meetings, every shareholder is entitled to speak, to ask questions and to propose motions directed against proposals of the management or the supervisory board regarding the items of the agenda. Shareholders are not required to notify the company in advance of such proposals. However, shareholders may use the company website in order to solicit support for their counter proposal. For that

purpose, shareholders representing 1 per cent of the company's share capital may:

- submit motions to agenda items, together with reasoning, up to a week prior to the meeting; and
- request that the proposals (including reasons) and the names of the proposing shareholders shall be uploaded to the company's website. The proposal must be received by the company at least seven business days prior to date of the shareholders' meeting.

The management board of the company (or the supervisory board in case of board or auditor elections) may render a statement to the proposal to be published on the website accompanying the shareholder motion. The company's managing directors are liable for damages occurring to the shareholders if the motion is not uploaded on the website. A resolution passed may also be contested by the minority shareholders on that basis. Motions will not be considered by the company for publication only in exceptional circunmstances, in particular, if they lack a written reason, would be unlawful or if the proposal would be defamatory or offensive under criminal law.

Amendment of the agenda of a shareholder meeting

Shareholder proposals concerning subjects other than items on the agenda are only admissible if the agenda is amended accordingly. Only shareholders individually or collectively that have been shareholders for at least three months and represent in total 5 per cent of the company's share capital may, in written form, request that additional proposals are included on the agenda of a shareholders' meeting (section 109, paragraph 1, AktG). This request must be received by the company 21 days prior to an ordinary or 19 days prior to the date of an extraordinary shareholders' meeting. An amended agenda has to be published in the same manner and form as the original agenda (for listed companies publication in the Federal Gazette, push forward media (eg, Bloomberg, Reuters or Newswire) as well as on the company's website). To pursue their rights, shareholders may request the convening of an additional shareholders' meeting, which can then be enforced in court.

Ordinary subjects of shareholder resolution proposals are:

- counterproposals on profit distributions;
- alternative or additional supervisory board candidates;
- special audit by appointing a special auditor;
- the enforcement of certain compensation claims against board members or other persons; and
- the appointment of special representatives to enforce these claims.

The shareholders' meeting is competent only as far as expressly provided for by corporate law or by the AoA. The AktG provides mandatory competence of the shareholders' meeting on the following items:

- approval of the annual accounts if the supervisory board did not approve or if the management board as well as the supervisory board decided to entrust the shareholders' meeting to resolve upon the issue (section 104, paragraph 2, lit 1, AktG);
- appropriation of distributable profits (section 104, paragraph 2, lit 2, AktG – please note that the profits shown on the balance sheet have to be fully distributed unless the AoA allows a full or partial retention by shareholder resolution);
- adjournment of the shareholders' meeting (section 104, paragraph 2, lit 3, AktG);
- discharge of the members of the management board and supervisory board;
- appointment and removal of supervisory board members (section 87, AktG);
- compensation of the supervisory board members (section 98, AktG);
- appointment of the company auditor (section 270, paragraph 1, Austrian Commercial Code);
- issuance and authorities for issuance of convertible or profit participating bonds (section 174, paragraph 1, AktG) or participation rights (section 174 para 3 AktG);
- amendment of the AoA (section 145, paragraph 2, AktG);
- capital measures, including authorisations to the management to increase the share capital;
- management matters brought to the shareholders' meeting by the management board or supervisory board (the latter as far as subject to supervisory board approval) (section 103, paragraph 2, AktG);
- decisions of major importance for the company such as major divestments, drop-down acquisitions (based on adopted German case law known as the Holzmüller/Gelatine-doctrine);
- mergers, demergers and certain other corporate restructuring measures;
- squeeze-out;
- vote of no-confidence in respect of members of the management board (section 75, paragraph 4, AktG);
- special audit and appointment of a special auditor (section 130 paragraph 1, AktG);
- profit-pooling agreements (section 238 para 1 AktG);
- delegation or lease of the operation of the company's commercial activities or the acceptance of such delegation or lease in respect of another company (section 238, paragraph 2, AktG);
- transfer of the entire assets of the company (section 237, paragraph 1, AktG);
- dissolution of the company (section 203, paragraph 1, lit 2, AktG) and continuation of a dissolved company (section 215, AktG);
- appointment and removal of liquidators (section 206, AktG); and
- discharge of the liquidators (section 211, paragraph 2, AktG).

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

If an item of the agenda in a shareholders' meeting, any shareholder (group of shareholders) representing 1 per cent of the share capital of a listed company, can propose candidates for election to the supervisory board. For that purpose, the details of proposed candidates for the supervisory board have to be submitted (including a declaration of the candidate according to section 87, paragraph 4, AktG) requesting an upload to the company's website together with the names of the proposing shareholders (section 110, paragraphs 1 and 2, AktG). Such a proposal must be received by the company at least seven business days prior to date of the shareholders' meeting. The supervisory board may render a statement with respect to the proposal to be published on the website accompanying the shareholder proposal.

In the case of listed companies, only candidates presented on the company's website on the fifth business day prior to the shareholders' meeting at the latest qualify for an election to the supervisory board. No candidates can be proposed ad hoc in the shareholders' meeting of a listed company (section 87, paragraph 8, AktG).

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Request to call a shareholders' meeting

Shareholders who together hold at least 5 per cent of the share capital (or less if stated in the AoA) may require the company to call a shareholders' meeting (section 105, paragraph 3, AktG). The request has to be addressed to the management board in writing and should state the objective and reasons together with an agenda and motions for each

agenda item. Requesting shareholders must prove that they hold a sufficient number of shares (quorum) for the legally required minimum period of ownership of three months. The shareholding, including the holding period of three months, may be evidenced by a deposit confirmation (or in the case of registered shares by an entry in the share register).

Permission to call a shareholders' meeting at the company's expense

If the company fails to comply with a proper request to call a shareholders' meeting, requesting shareholders may apply to the court for an authorisation to call a shareholders' meeting at the company's expense (section 105, paragraph 4, AktG).

Shareholders' meeting required:

Shareholders may not act by written consent in lieu of a shareholders' meeting.

Litigation

10 | What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Each shareholder may request at a shareholders' meeting to resolve upon an appointment of a special auditor investigating actions of the management. The purpose of the special audit is to obtain information on any breaches of duty. This information might be necessary to bring an action, especially as the plaintiff bears the burden of proof. In case such resolution is not passed a shareholder (or group of shareholders) holding 10 per cent of the share capital (over the last three months) may request a special audit and appointment of a special auditor at court, provided that the shareholders are able to demonstrate evidence that the company has been harmed.

The assertion of damage claims by the company against shareholders, members of the management board or the supervisory board, can be requested by a shareholder (or a group of shareholders) holding 10 per cent of the share capital (over the last three months until the legal proceedings have been completed), if such claims are not manifestly unfounded. The threshold to request the assertion of damage claims by the company is reduced to 5 per cent of the share capital, if a report by special auditors reveals a potential basis of liability.

In Austria, strike suits by professional plaintiffs seeking profits through litigation are not very common. The general idea is to block (delay) the registration of a shareholder resolution with the commercial register (eg, capital increases, merger, spin-off) as they become effective only upon registration with the commercial register. The commercial register court may decide to suspend the proceedings to register a shareholder resolution in the case of a pending challenge. However, the court would also have the discretion to register the shareholder resolution irrespective of the pending suit, if the interest of the company in the transaction outweighs the interest pursued by the claiming shareholder. The cost risk of litigation, however, often deters shareholders from raising such claims.

Further, the challenge of a shareholder resolution on restructurings (such as mergers) or a squeeze-out shall not be based on an alleged inadequate share exchange ratio of merger or squeeze-out compensation. Those may be examined in a special court procedure, which may lead to additional compensation payments (or the granting of additional shares in case of a merger) without, however, blocking the registration with the commercial register and delaying the transaction.

Austrian law does not provide for class actions. However, depending on the subject matter, models based on private law agreements have been developed, involving assignment of claims to claimant vehicles including financing by litigation finance providers.

There is no comprehensive right to obtain information or the right to inspect the company's books; rather, the right to obtain information and raise questions is exclusively concentrated on the shareholders' meeting.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 | Do shareholder activists owe fiduciary duties to the company?

Each shareholder owes a general fiduciary duty to the company as well as towards other shareholders; such fiduciary duty is based on case law and imposes certain limits on the power of the majority as well as on minority rights. Shareholders that influence members of the management or supervisory board to act against the interests of the company may be held liable for damages.

Compensation

12 | May directors accept compensation from shareholders who appoint them?

Members of the supervisory board are elected by the shareholders in the shareholders' meeting or by delegation of shareholders in the case that registered shares (golden shares) of a company carry such delegation rights. Members of the supervisory board are usually compensated by the company. However, they may accept direct compensation from shareholders under certain circumstances.

Whatever the case all duties of the supervisory board are primarily owed to the company (and not to the shareholders), regardless of whether a member receives direct compensation from shareholders or not. Members of the supervisory board that are in breach of their duties may be held liable under civil and criminal law.

Members of the management board are appointed by the supervisory board, which includes the determination of the remuneration of the board member (also payments from shareholders, as the case may be, are subject to the approval of the supervisory board).

Mandatory bids

13 | Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

Under the Austrian Takeover Act, a group of shareholders acting in concert must launch a mandatory offer to acquire the remaining shares in a listed company upon obtaining control (ie, a shareholding representing, directly or indirectly, at least 30 per cent of the voting rights (or a lower threshold provided by the AoA)). Certain exemptions are applicable: for example, another shareholder (group of shareholders acting in concert) holds the same or a higher percentage of voting rights. Shareholdings and voting rights of shareholders acting in concert are aggregated.

'Acting in concert' is defined as jointly seeking control of or exercising control over the company on the basis of an arrangement, not necessarily to be qualified as an enforceable agreement. A (rebuttable) presumption of acting in concert applies where the parties in question belong to the same group of companies or participate in arrangements regarding the election of supervisory board members.

Generally, the Austrian Takeover Commission closely scrutinises any contact between major shareholders on the appointment and removal of supervisory board members and other sensitive measures that are considered as 'control seeking', if the aggregated shareholding of the shareholders exceeds 30 per cent. In order to determine a group of shareholders acting in concert, a broad range of indicative behaviour is considered by the Austrian Takeover Commission. In particular, this concerns any communication (eg, written, oral, tacit) by a shareholder that can reasonably be expected to cause another shareholder to exercise its voting or other shareholder rights in a particular manner as an arrangement (irrespective of a binding effect). Recently, the Austrian Takeover Commission decided that an activist shareholder acting in concert with another (previously) non-controlling shareholder crossed the threshold of 30 per cent and violated its obligation to launch a mandatory offer.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Under the Austrian Stock Exchange Act, a shareholder must publicly disclose its shareholding to the Austrian Financial Market Authority, the Stock Exchange and the issuer, if it reaches, exceeds or falls below 4, 5, 10, 15, 20, 25, 30, 35, 40, 45, 50, 75 or 90 per cent of the voting rights of the company, either directly or indirectly (eg, via subsidiaries) or through financial instruments or derivatives through which voting shares can be acquired or instruments that have a similar economic effect. For the purpose of determining whether a threshold has been reached, voting rights from shares and instruments are aggregated. The AoA may include a further disclosure threshold at 3 per cent. A shareholder must make the disclosure immediately and in any event within two trading days, and each time its shareholding meets, exceeds or falls below a relevant threshold.

Shareholders acting in concert are aggregated for the purposes of compliance with disclosure thresholds.

Shareholders are not obliged to reveal their intentions or investment strategy in such disclosure. Nevertheless, a disclosure requirement with respect to investment strategies can arise from other disclosure obligations shareholders may be subject to, for example, if shareholders are to be qualified as investment funds or stock-listed companies themselves.

Non-compliance with disclosure obligations results in an automatic suspension of voting rights attached to the shares not disclosed (the AoA may generally extend such suspension to all voting rights of the non-compliant shareholder). The voting rights can be exercised again after a period of six months following due disclosure of the shareholding.

A violation of disclosure obligations can result in an administrative fine of up to €2 million or twice the amount of the benefit derived from the violation, whichever amount is higher. Administrative fines are published online as part of 'naming and shaming'.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

The disclosure requirements cover not only the acquisition and sale of shares, but also derivative financial instruments such as call-options, shares in investment funds and similar instruments.

Law provides for additional attributions according to which the shareholder must also report voting rights he or she can exercise or influence although they are arising from shares held by third parties. One of these attributions is 'acting in concert'. 'Acting in concert' means that the voting rights of the jointly acting legal entities are attributed to each other and must therefore be disclosed by each participating shareholder.

Short positions are not subject to large shareholder disclosure requirements.

Based on Regulation (EU) No. 236/2012 on short selling and certain aspects of credit default swaps, a two level transparency system was implemented for net short positions in shares: Net short positions in shares that reach 0.2 per cent of the issued share capital of the company have to be notified with the Austrian Financial Market Authority (FMA). If the net short position in shares reaches 0.5 per cent of the issued share capital, a respective publication on the website of the FMA is required.

Insider trading

16 | Do insider trading rules apply to activist activity?

Shareholder activists are also subject to the provisions on the prohibition of insider trading.

An activist strategy may be qualified as inside information. If this is the case, it has to be noted that in general the shareholder activists are not limited to use their 'self-created' inside information themselves. On the other hand, if the management is aware of an activist strategy to be qualified as an inside information, the management has to meet the obligations for the public disclosure of inside information.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

Structural strategies preventing or hindering shareholder activism are:

- issue additional securities to increase the costs of a takeover offer; and
- stagger terms of members of the supervisory board.

Requiring a change to the articles of AoA or shareholder resolution:

- higher voting thresholds or additional voting requirements compared to the statutory voting requirements;
- right of certain shareholders (holders of registered shares) to nominate supervisory board members;
- decrease of the threshold for the attainment of a controlling interest leading to a mandatory takeover bid;
- voting caps; and
- issuing of dual-class stocks whereby a maximum of one-third of shares can be issued without voting rights (preference shares); and
- delisting.

Of course, such defences do not protect the company against the exercise of minority rights with the intent to levy pressure on the management. They, however, make the formation of minority shareholder groups or the accumulation of shares in the hands of the activist share-holders less likely.

Structural features making a company more likely to come under the influence or be targeted by activist shareholders are:

- a large number of free-floating shares;
- passive institutional shareholders;
- low attendance in shareholders' meetings;
- depressed or discounted stock price; and
- takeover or restructuring situations (supporting or rejecting takeover bids or blocking of shareholder resolutions).

In respect of takeover situations, the board neutrality rule has to be observed. Once the target company gains knowledge of a bidder's intention to launch a bid ('relevant date'), the company must not take

measures that could impair the shareholder's opportunity to make a free and informed decision on the offer and, further, the target company's management (as well as the supervisory board) must obtain the consent of the shareholders' meeting for any measures (other than seeking alternative bids) that could impair the takeover bid, such as issuing of securities that could prevent the bidder from acquiring control of the target company, sale of material assets ('crown jewels'), purchase of other companies or businesses or material changes to the financing structure. No shareholders' meeting consent is required for the implementation of board decisions:

- in the ordinary course of business that were taken prior to the relevant date;
- that have been (at least partially) implemented by the relevant date; or
- for any measures the board is already obliged to take at that time.

Preparation

18 What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

Although shareholder activism has increased in recent years, it is still a rather new phenomenon in Austria and does not have the same impact as in other jurisdictions. To be prepared for shareholder activism, companies should analyse their business model and their shareholder structure from the perspective of an activist shareholder.

The following measures should be considered:

- engage in an active dialogue with institutional shareholders on the company strategy in particular on potentially contentious measures;
- establish a process to supervise the media, rumours and the shareholder structure in order to be prepared for quick reactions
- appoint an 'action team';
- prepare investor and public statements (response strategy) in particular on any items likely to be addressed by activist shareholders;
- implementation of a 'one-voice policy';
- decrease the threshold for disclosures of significant shareholdings to 3 per cent (change of the AoA); and
- extend the suspension of voting rights attached to the shares on all voting rights of a shareholder infringing disclosure rules for significant shareholdings (change of the AoA).

Defences

19 What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

The following defence measures should be considered:

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- decrease the threshold for disclosures of significant shareholdings to 3 per cent (change of the AoA); and
- extend the suspension of voting rights attached to the shares on all voting rights of a shareholder infringing disclosure rules for significant shareholdings (change of the AoA).

If the company has become the target of the activist shareholder, the following procedure is recommended:

- elaboration of a coordinated communication or reaction of the company;
- careful preparation of rapid responses to avoid uncertainty among market participants;
- avoid the impression that the activist shareholder is pursuing a new strategy in the interests of shareholders and society as a whole;
- countering with facts and reasonable, economically and legally sound answers; and
- strong and positive business development as best defence reaction.

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

There is no statutory proxy voting outside the shareholders' meeting. Shareholders may participate in shareholders' meetings by way of electronic communication if the company's AoA provide for such participation. If a proxy voter is nominated, voting instructions given to the proxy voter are often kept confidential and, in general, there is no exchange between management and shareholders on such instructions submitted prior to the shareholders' meeting.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

In general, it is not common to enter into a private settlement. If a settlement is considered, the management is obliged to examine and assess activist shareholder's requests in detail. An unconditional advance commitment is inadmissible in any case.

In particular, the management has to examine whether the activist shareholder's proposal is in the interests of the company, the other shareholders and the enterprise. A settlement with respect to individual proposals of the activist shareholder (eg, disinvestment of participations, change of dividend policy, proposals for appointments to the supervisory board, etc) is permissible if the proposals are in the best interests of the company and the agreement is made subject to change of circumstances.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

In the recent past, the engagement of Austrian listed companies regarding shareholder communication increased significantly. Besides investor relations activities, roadshows, investor conference calls and press conferences, the management also liaises individual institutional investors or groups. In any case, the management has to comply with the principle of equal treatment of all shareholders (section 47a, AktG) as well as the obligation to keep the company's affairs confidential. Nevertheless the communication with activist shareholders is legally permitted if it is in the interests of the company and its (other) shareholders.

23 Are directors commonly involved in shareholder engagement efforts?

In most Austrian companies, the members of the management board will primarily handle contact with significant shareholders or activists.

Also the management might be involved in shareholder engagement efforts and the further approach. Depending on the composition of the boards and the acting individuals, the chairman of the supervisory board may also be involved in a direct dialogue with significant shareholders or activists.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Selective disclosure to particular shareholders by the company outside of a shareholders' meeting has to comply with the principle of equal treatment of all shareholders (section 47a, AktG). The CGK also emphasises that institutional and individual investors have to be treated equally. Information disclosed outside of a shareholders' meeting is only admissible if it is in the interest of the company and if there is no unjustifiable preferential treatment.

Any such disclosed information must not qualify as inside information or be of disadvantage to other shareholders.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

Communication can be conducted by companies as well as activists via:

- open letters and campaigns;
- press conferences;
- website;
- letter;
- email;
- social media; and
- proxy fights via proxy advisers on motions for shareholder resolutions and contested director elections.

Recently, the EU Shareholders' Rights Directive (2017/828) has been amended providing the right of companies to have their shareholders identified, to register respective data and to address and communicate with shareholders.

There are no special legal provisions in connection with the use of social media; however, the general rules against market abuse have to be observed. See question 13 on the obligation of shareholders acting in concert to launch a mandatory takeover offer, disclosure requirements on significant shareholdings (question 14) and the board neutrality rule to be observed in respect of takeover situations (question 17).

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

In principle, non-listed stock corporations may only issue registered shares and must maintain a share register. The share register shall not be made available to the public or to other shareholders due to privacy requirements (data protection legislation). Listed stock corporations generally issue bearer shares and cannot maintain a shareholder register.

bpv HÜGEL

Christoph Nauer
christoph.nauer@bpv-huegel.com

Daniel Reiter
daniel.reiter@bpv-huegel.com

Donau-City-Straße 11
ARES Tower
1220 Vienna
Austria
Tel: +43 1 260 50 0
Fax: +43 1 260 50 133

Enzersdorferstraße 4
2340 Mödling
Austria
Tel: +43 2236 893377 0
Fax: +43 2236-893377 40

www.bpv-huegel.com

However, access to the list of participants of a shareholders' meeting (including the number of shares present at the meeting) can be derived publicly from the commercial register. The participant list has to be attached to the minutes of a shareholders' meeting filed with the commercial register (sections 117 and 120, paragraph 3, AktG).

Recently, the Economic Owner Register Act has been enacted concerning the transparency of beneficial ownership of companies, other legal entities and trusts have to be registered in a register. This register, however, is not a public register. Only persons who may produce a legitimate interest concerning the prevention of money laundering and terrorist financing are allowed to inspect the register.

The EU Shareholders' Rights Directive (2017/828) has been amended providing the right of companies to have their shareholders identified, to register respective data and to address and communicate with shareholders. However, any such company data will not be accessible to (activist) shareholders.

According to the CGK, the company is obliged to hold regular conference calls or events for analysts and investors. The CGK ensures that the same information is made public following a communication to financial analysts or investors. The rule addresses new facts and thus covers all new information, irrespective of its price relevance and importance. The provision thus goes well beyond the mandatory duty programme of the Market Abuse Regulation.

Brazil

Carlos Portugal Gouvêa and Caio Henrique Yoshikawa
PG LAW

GENERAL

Primary sources

1 | What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

Brazilian Corporations Law (Law No. 6,404 of 1976), Brazilian Capital Markets Law (Law No. 6,385 of 1976) and regulations issued by Brazilian Securities and Exchange Commission (CVM) are the primary sources of laws and regulations on shareholder activism and engagement. Self-regulatory rules issued by the Brazilian stock exchange (B3) applicable to companies registered on its special listing segments related to disclosure of information to shareholders, dispersion and restriction on issuance of non-voting shares, and mandatory arbitration procedures are also relevant to shareholder engagement.

Enforcement of Brazilian laws on shareholder activism is incumbent upon the judiciary branch and the CVM. However, the latter has a leading role in building the case law on disputes on shareholder activism as an administrative body responsible for the enforcement of Brazilian Corporations Law, Brazilian Capital Markets Law and the CVM rules for public companies. Administrative penalties imposed by the CVM may vary from formal warnings to substantial fines and prohibition of holding offices in public companies in Brazil. It may be applicable to officers, directors, members of the board of supervisors and shareholders. B3 as a self-regulatory body is responsible to impose penalties for breach of its rules. Public corporations registered before certain special listing segments provided by B3, namely Novo Mercado, Nível 2, Bovespa Mais, and Bovespa Mais Nível 2, must have a mandatory arbitration referring to a specific arbitration chamber supported by B3, the Câmara de Arbitragem do Mercado (CAM). For all others, it is optional to adopt arbitration provisions before CAM and a limited number of public companies made such option. Under Brazilian corporate law, arbitration provisions included in the corporations' charter are regarded as enforceable and binding to all past, present and future shareholders of the company.

Shareholder activism

2 | How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Shareholder activism is still under development in Brazil. Until very recently, shareholder activism was not common in the Brazilian market. The reasons for that are related to certain features of Brazilian corporate law with regards to derivative lawsuits, which put a substantial burden on minority shareholders that eventually start the lawsuit, and with regards to class actions, which has an unfavourable case law. Therefore, shareholders rely heavily on representations before the CVM as an initial step before a damages civil lawsuit. The overall environment is unfavourable toward activist campaigns, but there has been pressure for change due to the different treatment provided to investors on deposit receipts of Brazilian companies negotiated in other jurisdictions. There have been very public cases in which foreign investors holding deposit receipts obtained indemnification awards in foreign jurisdictions while investors in the Brazilian market were not successful, despite filing lawsuits based on substantially the same facts.

3 | How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

Shareholder activism is increasingly viewed in Brazil as a relevant mechanism for the enforcement of best corporate governance practices in public companies. We expect Brazilian courts to change its current case law towards more favourable interpretations of current statutes to minority shareholders, aligning the legal environment in Brazil with other leading jurisdictions.

Brazil does not present a pattern of shareholder activism targeted at specific industries. A high or low incidence of shareholder activism depends on the concentration of ownership of each company. Most recently, due to the changes in the anti-corruption, anti-money laundering and anti-organised crime legislation, a series of corruption scandals erupted. Investigations also resulted in shareholder activism against companies involved in these scandals due to false information provided to investors. However, such investigations reached companies in many sectors, such as construction, oil and gas, food products and financial institutions.

4 | What are the typical characteristics of shareholder activists in your jurisdiction?

Compared with jurisdictions where most of share ownership is dispersed, shareholder activism in Brazil is not a widespread practice. Most Brazilian public companies have a high degree of ownership concentration and, as a result, threats to management through takeovers is quite limited. In Brazil, the leading shareholder activists are pension funds of state-owned companies, investment fund managers, experienced individuals and other institutional investors as minority shareholders. Investor associations are becoming stronger and more engaged on efforts to improve corporate governance and on developing capability to support class actions. The main tool that has been used by activists is the filing of representations and complaints before the CVM to investigate misconduct of managers and controlling shareholders.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

From an internal point of view, shareholder activism focuses on overseeing companies' internal controls. Activists also focus on the compliance with the law of relevant transactions and material changes in the company (eg, corporate reorganisations). On the other hand, recent corruption scandals and environmental disasters have recently drawn the attention of minority shareholders claiming indemnification for losses related to depreciation of the high-profile companies' stock price.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

Activist shareholders normally make joint efforts to appoint members to the board of directors and board of supervisors of companies. Shareholders representing at least 15 per cent of voting capital or preferred shareholders representing at least 10 per cent of the total capital are entitled to appoint one member of the board of directors. Minority shareholders representing at least 10 per cent of the voting capital may appoint a member of the board of supervisors and require cumulative voting in director elections. Appointing members of the board of directors and of the board of supervisors allows them to have easier access to information on the issues to be discussed at the shareholders' meeting and a better oversight of management, since members of the board of directors may request that certain decisions are subject to approval of the General Shareholders' Meeting, members of the board of supervisors have broad powers to obtain information from the company's officers, participate in the General Shareholders' Meeting answering questions of the shareholders and can also provide individual reports to the General Shareholders' Meeting. In addition, activist shareholders often file administrative representations and complaints against management or controlling shareholders' decisions or relevant transactions approved by shareholders meetings with the CVM.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

Shareholders' meetings are divided in two types: the ordinary meeting and the extraordinary one, depending on the matters to be discussed. The ordinary shareholders' meeting is mandatory and should be held up until April of every year, takes place annually and can be held exclusively to discuss the matters proposed restrictively by the law, that is, approval of management accounts and financial statements, election of board members or officers, as applicable, and board of supervisors' members and destination of the net profit and dividends. Extraordinary shareholders' meeting can be held at any time of the year and shareholders can discuss any matters.

After the shareholders' meeting is organised, any shareholder may make a voting proposition regarding any topics of the agenda different from what is proposed by the controlling shareholder or management. Shareholders may not make proposals to include new topics in the agenda of the meeting unless all shareholders attend the meeting, what is virtually impossible in a public company.

The CVM regulated remote voting in shareholders' meetings to increase attendance, particularly of minority shareholders. Such rules are applicable only to public-listed companies. The public company shall mandatorily issue the distance voting ballot on ordinary shareholders' meeting, when the meeting is called to appoint managers, and when an extraordinary shareholders' meeting is called simultaneously with an ordinary shareholders' meeting. Shareholders of public companies can request that proposals are included in the ballot if their shareholding surpasses certain thresholds of the total capital provided by the CVM rule, ranging from 5 per cent to 10 per cent depending on the size of the total capital of the public company.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Yes, any shareholder may nominate candidates for the election of members of management at a shareholders' meeting. On companies with a board of directors, including all public companies, minority shareholders holding at least 15 per cent of voting capital or preferred shareholders representing at least 10 per cent of the total capital may request a segregated election to appoint one member of the board of directors as a representative of minority shareholders. Regarding the use of the company's proxy by public companies, according to CVM's rules, if the public company makes a proxy public request, shareholders holding at least 0.5 per cent of the share capital may appoint candidates if they notify the company of such intention up to five business days after the company makes public its intention to request a public proxy. If the public company requests a public proxy, it shall bear all costs of the proxy. Also, according to CVM rules, it is mandatory for the company to provide means for shareholders to vote remotely at shareholders' meetings called to discuss almost all cases that involve the election of members of the board of directors, and absolutely all elections of members of the supervisory board.

With regard to general proposals, shareholders of public companies can also request that candidates are included in the ballot if their shareholding surpasses certain thresholds of the total capital provided by the CVM rule, which for the inclusion of candidates only is based on a reduced shareholding threshold of 2.5 per cent to 0.5 per cent depending on the size of the total capital of the company, which is about half of the amounts requested for the inclusion of general proposals in the ballot. To initiate a proxy fight, any shareholder holding at least 0.5 per cent of the share capital may request a list of the addresses of all shareholders. The company cannot charge the shareholder any fees for providing such information. However, if the shareholder wants to start a proxy fight based on such a list and the company does not present a proxy public request, the shareholder must bear the costs of the proxy public request.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

The board of directors must call the shareholders' meeting. Otherwise it is incumbent upon the board of officers. Nevertheless, any shareholder may call a shareholders' meeting if the managers delay the call for more than 60 days of the term provided by the law or by the company's by-laws.

Shareholders owning at least 5 per cent of the voting capital of the company may call a shareholders' meeting when managers delay the call for more than eight days after they received a notice with justified request for a shareholders' meeting from such shareholders. Such notice shall include the list of proposals to be included in the agenda. If the managers delay the call of a shareholders' meeting to setup a board of supervisors for more than eight days, shareholders owning at

least 5 per cent of the voting capital of the company may call a shareholders' meeting.

Shareholders may not act by written consent, except where:

- all shareholders participate through the remote voting system in the public companies that adopt the remote voting system as regulated by CVM; or
- it is possible to gather the consent from shareholders representing 100 per cent of the voting capital of the company, with or without unanimous resolutions, what is more common in private companies.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Brazilian law provides judicial remedies such as:

- action to hold the company responsible for losses caused to stakeholders, including shareholders, by irregularities in the company's registers and books; and
- action to compel the company to show its registries, books and records.

Derivative actions against managers by the company depend on prior approval by the shareholders' meeting. If the company does not file the lawsuit against the managers within three months as of the approval by the shareholders' meeting, any shareholder can file such lawsuit in the name of the company. If the shareholders' meeting does not approve the filing of a lawsuit against the managers, shareholders representing at least 5 per cent of the share capital may file a derivative suit. In addition, controlling shareholders may be liable for abuse of power or conflict of interest.

A widespread way of litigation is filing requests for the CVM to decide at the administrative level on breach of legal and regulatory provisions and regulations by managers and controlling shareholders of public companies. In Brazil, class actions may be filed by the CVM and the public prosecutor office to protect investors in the securities markets, including minority shareholders.

Class actions brought by minority shareholders are uncommon in Brazil. Prosecutor offices can file class actions on behalf of shareholders to obtain indemnification for damages resulting from capital markets investments. However, there has been no record of any successful class action and none of the several prosecutor offices have been engaged on such litigation.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

Brazilian law does not provide specific fiduciary duties for shareholder activists. They are applicable only to controlling shareholders, directors and officers. However, shareholder activists may be held accountable for losses resulting from their action owing to the abuse of right doctrine. Also, all shareholders, including minority shareholders, are subject to broad conflicts of interest restrictions with regard to their votes at shareholders' meetings and minority shareholders might be subject to litigation claiming damages.

Compensation

12 May directors accept compensation from shareholders who appoint them?

The most common situation is the compensation to be paid directly from the company to the director, as a member of the board of directors. However, it is possible for directors to receive direct compensation from a shareholder who appointed them. In many of such cases, the director waives the payment directly from the company.

Payments by the controlling shareholder to the directors as well as any compensation paid for other types of services provided by the relevant director shall be disclosed to the market according to CVM disclosure rules.

Mandatory bids

13 Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

Brazilian Law requires that the acquirer of the control of a company makes a tender offer for all the remaining voting shares of the company for the price per share of at least 80 per cent of the price per share offered to the seller of the controlling shareholding. Rules of Novo Mercado, the listing segment at B3 with the higher standards of corporate governance, the Nivel 2, Bovespa Mais and Bovespa Mais Nível 2, require that such a tender offer for the shares of all the remaining voting shareholders to be 100 per cent of the price per share offered to the seller of the controlling stake.

Another event of mandatory bid requirement is if the controlling shareholder acquires, by any means other than through a tender offer, more than a third of the outstanding shares of the public company in the securities market (free float). In this case, the controlling shareholder is subject to a tender offer for the remaining outstanding shares the valuation of which will be conducted by an independent appraiser.

As a rule, minority shareholders either acting alone or in concert with other shareholders are not subject to mandatory bid requirements. However, 'poison pill' statutory clauses may result in the event of mandatory bid if a percentage provided in the by-laws is triggered by a group of shareholders acting as a group, depending on the specific 'poison pill' provision.

Disclosure rules

14 Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Yes. This obligation is applicable to direct or indirect controlling shareholders, shareholders who elect members of the board of directors or board of supervisors, any individual, entity or group of persons acting together or representing the same interest, which conduct material transactions (acquisitions and dispositions that changes the shareholding in multiples of 5 per cent) shall send to the company's investor relations officer, immediately after the completion of such transactions, information on, among other things, name and particulars, indication of any agreement with rules on voting rights and trading of securities issued by the company, number of shares and of other securities and derivatives indexed in such shares, with the amount, class and species of the related shares.

Shareholders must disclose the purpose of the shareholding, interest aimed and, as the case may be, a statement by which the shareholder declares that the transaction does not aim to change the control or the management structure of the company. Otherwise, it must be

disclosed to the market by the acquirer through the same ways used by the company.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

The disclosure requirements are applicable to derivative instruments, even if there is no physical settlement, according to the following rules:

- shares directly held and those referenced by derivatives cleared on a physical settlement shall be considered together to verify the percentages of shareholding disclosure;
- shares referenced by derivatives with an expectation of an exclusively financial settlement shall be calculated independently of the shares referred to in previous item to verify the percentages of shareholding disclosures; and
- the number of shares referenced in derivatives instruments that provide economic exposure to the shares cannot be offset by the number of shares referenced in derivatives that produce inverse economic effects.

Insider trading

16 | Do insider trading rules apply to activist activity?

Regardless of the activity, insider trading rules apply according to the subject when using relevant information not yet disclosed to the market to obtain undue advantages. Therefore, insider trading rules may apply to activist activity if it involves relevant information not yet disclosed to the market. If such information involves litigation activity, particularly considering that certain public companies adopted arbitration provisions regarding corporate litigation, which also include non-disclosure provisions, any negotiations of stock by a minority shareholder while holding non-public information with regard to litigation against the company, its controlling shareholders or management may be regarded as insider trading.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

Fiduciary duties according to Brazilian law include duty of care, duty of loyalty, duty of secrecy, and duty to inform, as applicable. There is no different standard for directors to fulfil their fiduciary duties when considering an activist proposal. According to Brazilian law, directors and officers always must act exclusively on behalf of the company's interest. However, the law provides that the disclosure of the acts or facts by the director at request of the shareholders may only be used in the legitimate interest of the company or the shareholder. In case of abuse of right by the activist shareholder, he or she may be liable for the request of information.

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

The safest way to minimise the risks is to adopt a complete and effective corporate governance and compliance programme. The law regarding penalties on administrative proceedings before the CVM has been recently changed to increase general penalties from up to 500,000 to 50 million reais. Therefore, public companies shall increase substantially their investments in compliance in order to prevent serving as examples to the market when the CVM starts using its new heightened supervision authority.

Having an effective compliance programme involves the adoption of best practices of disclosure, which includes providing information to the market in a concise, complete and accurate way, and consistent performance as well. Material facts, policies applicable to related party transactions, internal controls are important strategies for a good relationship with minority shareholders, including activists. If a company is guided by clear and well-known polices and complies with its disclosure duties, the shareholder's mistrust of the company's management and controlling group tends to reduce.

There is no official quantitative data available to enable us to establish in a broad sense whether shareholder activism is a matter of heightened concern in the boardrooms of Brazilian public companies. However, minority shareholders such as investment fund managers, pension funds of state-owned companies, experienced individual investors and state-owned investment funds may have a significant influence on the removal of managers or adoption of specific policies.

Considering that most recent shareholder litigation has focused on corruption, it is highly advisable that public companies should have strong anti-corruption and anti-money laundering compliance programmes.

Defences

19 | What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Brazilian capital markets have a structural defence against shareholder activism, which is a substantial concentration of corporate control. Most companies have a well-defined control group, by families or government. As a result, any shareholder activism focused on changing management would not be able to succeed without the participation of the controlling group.

Although Brazilian law prevents the issuance of multiple-voting shares, there are other structural mechanisms to enhance the power of the controlling group as a defence against shareholder activism. Brazilian law allows corporations to issue preferred shares without voting rights provided that the total amount of such shares does not surpass 50 per cent of the total number of shares of the company. However, listing segments with a higher level of corporate governance at the B3 forbid public companies from issuing non-voting shares (eg, Novo Mercado) or provide additional rights to non-voting shareholders (Nível 2), such as voting rights on major matters such as transformation, merger, spin-off or consolidation, approval on agreements between the corporation and the controlling shareholder and choice of specialised company for the valuation of the corporation.

Another tool that has been used is the inclusion of 'poison pill' provisions in the by-laws of a company to discourage a potential hostile takeover. The most common type of 'poison pill' is related to the mandatory tender offer of all the shares of the company held by the other shareholders if a shareholder acquires or becomes the holder of a certain percentage of the stock capital of the company as provided in such a 'poison pill'. In this case, the tender offer is subject to a price or a criterion already set forth in the 'poison pill' provision. Such prices usually include a very high premium that may jeopardise the efforts of activists to acquire relevant stockholdings.

Arbitration provisions in the charters may be regarded as a defence against minority shareholder litigation. Such provisions are required for public companies listed in the Novo Mercado, Nível 2, Bovespa Mais

and Bovespa Mais Nível 2, and optional for other public companies. However, many companies choose arbitration instead of subjecting themselves to the courts since arbitration provides further confidentiality to the dispute. CAM's case law is not public and presents much higher costs for minority shareholders to initiate disputes.

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

Brazilian law does not provide for a periodic or daily report requirement of proxy votes for the company. However, CVM rules on remote voting provides that the register agent of the shares must forward to the company two documents. These are:

- an analytic document with voting statement of shareholders duly identified with the extract of corporate shareholdings; and
- a summarised document with voting statement of shareholders, specifying how many approvals, refusals or abstentions on each subject and how many votes each candidate or list of candidates had received.

Such information must be delivered to the public company 48 hours in advance of the holding of the relevant shareholders' meeting.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

There is no public information in this regard. As mentioned before, certain special listing segments at B3 require a provision of arbitration clause in the companies' charter. Considering the high costs of initiating an arbitration procedure in Brazil, the existence of an arbitration clause eventually pushes activists, directors and controlling shareholders into negotiations before the filing of an arbitration request.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

There is an increasing number of associations of investors in the securities markets in recent years and international proxy companies such as ISS and Glass Lewis, which organise engagement of minority shareholders, especially against managers and controlling shareholders, are becoming more active and making proxy requests and remote voting more common, following on new rules regarding those matters issued by the CVM. However, due to the concentrated ownership of Brazilian public companies and the prominent role of institutional and state-owned enterprises, joint engagement of minority shareholders is not a widespread practice.

23 Are directors commonly involved in shareholder engagement efforts?

Members of the board of directors appointed by the activist minority shareholder or group of minority shareholders have led or supported engagement efforts. However, the directors owe fiduciary duties to the company and not to the shareholders who appointed them. Therefore, they must always act in the best interests of the company. If such goal is aligned with shareholder engagement, directors have no restrictions on joining such efforts.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

There are no specific rules on shareholders' communication with the board. Brazilian law provides that directors may be invited to provide explanations at shareholders' meetings. Brazilian laws and regulations provide the mandatory disclosure to the market of any material act or fact that may influence:

- the price of the securities issued by public companies or related to them; or
- the decision to buy, sell or hold such securities, or even to exercise any rights inherent to them.

'Material events' (including acts or facts) is, therefore, a broad concept, and certainly one that may include shareholder engagement efforts if they have influence in the pricing of securities. Selective or unequal disclosure are prohibited, since public companies have the duty to disclose such information through official channels of communication and to ensure its wide and immediate dissemination, simultaneously to all markets in which their securities are traded.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

Brazilian regulations for public companies set forth requirements for public requesting of proxies through media, such as newspapers, internet, radio and television. Such requirements are also applicable always if:

- the management or the controlling shareholders make such a request to more than five shareholders; and
- any other person makes such request to more than 10 shareholders.

If a company has an electronic system for proxies, shareholders representing at least 0.5 per cent of the stock capital may use such a system to conduct proxy public requesting. Proxy public request must include the draft power of attorney, the information provided in the CVM regulations, detailed information on the subject matters to be voted and any necessary documents as well. All materials sent in such public requests must be uploaded onto the CVM website to become available to all shareholders.

CVM regulations also provide rules for procedures and deadlines for remote voting and remote participation in the shareholders' meeting, which includes the authorisation for custodian and register agents to carry out the receipt and processing of the forms sent by shareholders in the case of distance voting. Companies may adopt electronic systems to allow remote participation in the shareholders' meetings subject to CVM specific rules.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

Any person may have access to the list of registered shareholders, provided that this access has the purposes of defending rights and clarify situations of personal interest or shareholders or the securities market, subject to pay any costs incurred by the company. In case of denial, the shareholder may appeal to the CVM.

In any case, the request shall identify:

- the right to be defended or the situation of personal interest to be clarified; and
- to what extend the disclosure of the list of shareholders is necessary for the defence of the right and clarification of the situation of personal interest.

In addition, the supply of the list of shareholders is applicable to situations where the right to be defended is inherent to the quality of shareholder. It means that, depending on the reasons for the request, the access may be granted by the company or the CVM only on a partial basis.

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

One major change that might influence shareholder activism in Brazil regards the increase in penalties potentially levied by CVM, the Brazilian capital markets authority. Since a majority of shareholder litigation in Brazil is performed through representations to CVM, higher penalties might provide further incentives for such representations and increase the bargaining power of minority shareholders. The law regarding penalties on administrative proceedings before the CVM has been altered to increase general penalties from up to 500,000 to 50 million reais, meaning a hundredfold increase in the capacity of CVM to penalise even simple compliance failures. For this reason, any public companies shall increase substantially their investments in compliance to prevent serving as examples to the market when the CVM starts using its new heightened supervision authority.

The most recent shareholder litigation has focused on corruption, and new cases are being presented every year. As a result, the pressure shall continue for public companies to implement strong anti-corruption and anti-money laundering compliance programmes. The anti-corruption statute (Federal Law 12.846/2013) and its regulations (provided by Presidential Decree 8.420/2015) provide a detailed framework of such compliance programmes and standards to evaluate their effectiveness as a means to reduce any future exposure of the public company.

Carlos Portugal Gouvêa
carlos.gouvea@pglaw.com.br

Caio Henrique Yoshikawa
caio.yoshikawa@pglaw.com.br

Avenida Nove de Julho, 3452
Conjunto 132
São Paulo
SP 01406 000
Brazil
Tel: +55 11 3085 0089
www.pglaw.com.br

France

Bertrand Cardi and Forrest G Alogna
Darrois Villey Maillot Brochier

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The most notable sources of laws and regulations relating to shareholder activism include French legislation (for example, the French Commercial Code (including European Directives as transposed into French law)), European regulations and Autorité des marchés financiers (AMF) regulations. Domestically, the French parliament and the AMF promulgate relevant law and regulations, which may be enforced by civil parties or the public prosecutor before the French courts or by the AMF through the AMF sanctions commission.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Campaigns involving French-listed companies have remained fairly constant in recent years, with approximately five to 10 public activist campaigns per year.

However, the aggressiveness of such campaigns has increased over time. For example, there has been a significant increase from 2014 to 2017 in the number of external resolutions proposed by shareholders. In 2017, 73 external resolutions were proposed by shareholders in nine companies, compared with 45 external resolutions in 12 companies in 2016, 30 external resolutions proposed in nine companies in 2015 and 13 external resolutions proposed in eight companies in 2014. This number dropped significantly in 2018, down to only 20 external resolutions.

Based on a review of activist campaigns since 2013, it appears that nearly one third result in at least a partial satisfaction of activist demands. However, as with any data set, much depends on how success is measured. More aggressive tactics may be markedly less likely to succeed. For example, of the 73 external resolutions proposed by shareholders in 2017, only six were adopted (8 per cent). In 2018, none were approved by a majority of shareholder votes.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

Popular consciousness of activism has increased considerably over the last decade.

The French legislature has promulgated several laws in recent years designed to limit the influence of short-term investors. For example, the government's draft of the PACTE Law, a law that is expected to be passed in April or May of this year, would reinforce the corporate interest (an independent interest attributable to the entity itself, and conjoining the interest of all corporate stakeholders) so that, in addition to the corporate interest, corporate decisionmakers are also required to take into account the labour and environmental implications of the corporation's activity. In addition, the new law would also introduce the possibility to include the corporate purpose, or the 'raison d'être', of the company in its articles of association. These reforms may in practice reinforce corporate defences against short-term objectives espoused by activists. The availability of double-voting rights for registered shareholders after two years is also designed to encourage a long-term vision.

French regulators have generally been tolerant – and at times sympathetic to – certain aspects of activism, particularly to the extent campaigns focus on good governance, rigorous disclosure and the interests of minority shareholders. However, this tolerance has not prevented the AMF from disciplining activist abuses, including insider trading, violations of disclosure obligations (for example, in the context of stake-building or misleading statements) and market manipulation. The AMF has done so even when the conduct at issue seeks to comply with the letter of the law.

Given the relatively small number of activist interventions in France, it is difficult to draw definitive conclusions about the industries most likely to be the targets of such attacks. French-listed targets have clearly grown larger in recent years (eg, Accor, Airbus, Carrefour, Danone, Safran and Vivendi). That being said, companies with a market capitalisation of between €500 million and €5 billion continue to be prime targets (eg, Euro Disney, Nexans, Rexel, SoLocal, Technicolor, XPO Logistics Europe, Scor and Pernod Ricard).

4 What are the typical characteristics of shareholder activists in your jurisdiction?

The key shareholder activists in recent campaigns in France include a number of well-known investors based in the United States, the United Kingdom and Europe such as Cevian Capital, Elliott Management, Knight Vinke, The Children's Investment Fund Management (TCI) and Trian Fund Management.

French native activists include both financial and industrial concerns, including in the former category Amber Capital (UK-based but with founders with strong French ties), Charity Investment Asset Management (CIAM), Phitrust, SFAM and Wendel and, in the latter category, LVMH in its acquisition of a significant position in Hermès. French associations of minority shareholders such as the Association for the Defence of Minority Shareholders and SOS Small Holders, continue to play a role, including in litigation, sometimes in partnership with other activists.

In addition, there has been a growing trend of more traditional institutional investors taking a more active role in their portfolios to agitate change, sometimes in tandem with activists.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

As regards operations, activists may focus on cost-cutting and reorganisations. For governance, activists may agitate for changes in management or at the board, including seeking the nomination of activist representatives or, increasingly, independent directors proposed by the activist. Activists are focused on M&A as a creator of value, whether in opposing announced transactions with valuations that they disagree with, or seeking to trigger transactions (including divestments) if they believe it will unlock value. Activists may also work in favour of dismantling anti-takeover defences and limiting majority shareholder advantages or perceived self-dealing.

Underperformance compared with peers, capital reallocation or return opportunities and M&A or break-up possibilities are key factors that may attract shareholder activist attention.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

At the highest level of abstraction, the classic activist intervention involves acquiring a minority stake in the target company by way of an economic interest (in the form of a direct acquisition of shares, through derivative instruments or even the acquisition of debt securities or other credit exposure) and attempting to pressure the board and management (including through the use of shareholder democracy) to seek to influence the company's stock price.

Within this framework, common activist strategies vary considerably depending on circumstances, but may include:

- seeking to add items to the agenda of a shareholders' meeting or propose new resolutions (Wyser-Pratte regarding Lagardère, TCI in Safran-Zodiac);
- criticising announced M&A transactions (TCI in Safran-Zodiac, Amber Capital as regards Gameloft SE);
- seeking board seats (Cevian in relation to Rexel, CIAM as regards Alès Group, Pardus Capital Management regarding Valeo, Pardus and Centaurus Capital in relation to Atos Origin, Financière de l'Echiquier and Sterling Strategic Value as regards Latécoère, Amber Capital as regards Lagardère, SFAM as regards FNAC Darty);
- seeking a court-appointed independent expert (Elliott in its countersuit against XPO);
- 'no' campaigns on executive compensation (the Hollande administration in relation to Alstom, Renault and Safran (resulting in 'no' votes in 2016 against the compensation of Carlos Ghosn and Patrick Kron, the CEOs of Renault and Alstom respectively));
- blocking a squeeze out (Elliott in both APRR and XPO Logistics Europe);
- orchestrating a public relations campaign, including letter-writing (including lobbying individual board members or relevant regulators), press interviews and lobbying of proxy advisers; and
- in relatively rare cases, threatening (TCI in Safran-Zodiac) or actually initiating litigation (CIAM in Euro Disney, CIAM against Altice).

From a purely financial perspective, activists have had increasing recourse to equity collars in connection with their stakes. This structure is adopted as a matter of stake-building (to avoid disruption in the stock price) – however, in the longer term, this tool may also be used to limit the activist's financial exposure to the target, disaligning the activist's economic interests from those of other shareholders (eg, as has been reported regarding Elliott in its Telecom Italia investment).

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

Shareholders that meet the applicable minimum shareholding threshold in a listed entity in France, as well as qualifying minority shareholder associations, may seek to add items for discussion to the agenda for any shareholder meeting or propose additional draft resolutions to be included in 'proxy' materials distributed to shareholders. The applicable minimum threshold depends on the share capital of the issuer and is calculated on a sliding scale. It cannot be more than 5 per cent; in the very largest companies, it may approach 0.50 per cent.

External shareholder resolutions may include, for example, major strategic or financial initiatives (such as an exceptional dividend, a share buyback or a spin-off), material governance changes (including a separation of the CEO and chairman roles or a resolution for a special committee of independent directors to be formed to undertake a strategic review of management's performance, compensation or succession planning) or various other disruptive proposals (eg, the transformation of the corporate form into a takeover-friendly structure).

However, in accordance with the fundamental principle under French law regarding the proper competence of the respective decision-making organs of the corporation, some boards have resisted the proposal to include an item that does not fall within the competence of the shareholders' meeting (eg, a change of strategic direction).

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Yes. In France, upon proposal of any shareholder, and irrespective of a director's term, any director may be removed and replaced at any shareholder meeting by a simple majority vote of the shareholders even if the matter is not on the meeting agenda. In addition, under the shareholder proposal right discussed above, a draft resolution proposing the removal and replacement of any director may be included in the company's proxy materials circulated to shareholders in advance of a shareholder meeting.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Shareholders holding 5 per cent as well as certain minority shareholder associations may request the president of the commercial court to convene a shareholder meeting in the event that the company has failed to call the relevant meeting following a specific request. The court assesses whether the request is for legitimate purposes and in the corporate interest of the company, and not solely to satisfy the plaintiff's personal interests. If the request is granted, the court sets the agenda and appoints an agent to convene the meeting.

Shareholders of French listed companies are not permitted to act by written consent in lieu of a meeting.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

While shareholder litigation is relatively unusual in France, shareholders recourse is available against corporations and directors. For instance, shareholder litigation can be commenced on the merits by way of derivative action (action sociale ut singuli). Derivative suits may not be pursued as a class action, as this procedure is not available under French law with respect to shareholder claims. The cost of the derivative suit is borne entirely by the shareholder, while any recovery is allocated to the company. A personal cause of action is also available; however, the plaintiff must demonstrate that the relevant loss is personal to him or her, and distinct from any loss incurred by the company or the other shareholders.

Other litigation, such as based on an abuse by majority shareholders, criticism of insider transactions, seeking the liability of managers or seeking redress for procedural failings, may also be available to activists.

There are also a variety of criminal actions available in France in connection with corporate conduct; however, such actions depend on the relevant authority exercising its prosecutorial discretion to elect to actively pursue the matter.

Shareholders have certain general information rights that generally only concern public documents and information that must in any event be publicly communicated. An additional and much broader right available generally under French civil procedure also permits 'any interested party' (including a minority shareholder) to seek, on an ex parte basis, the seizure of evidence that may be necessary for contemplated litigation.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

Shareholders do not owe any fiduciary duties to the company per se but they have an obligation not to abuse their position by way of oppressive action (often, a hostile vote) or inaction (eg, abstention from a vote) wrongfully designed to benefit certain minority shareholders and that is contrary to the company's corporate interest.

Compensation

12 May directors accept compensation from shareholders who appoint them?

Although no French court has considered the question, it does not appear that such a compensation scheme would in and of itself violate any statutory provision of French law. However, such a scheme would clearly be problematic in practice to the extent it were to interfere with a director's duty to act in good faith and to put the interest of the company ahead of any personal interest, as well as the director's duty to take decisions with as sole consideration the company's corporate interest. The director would also need to comply with applicable confidentiality obligations, significantly limiting his or her ability to communicate and coordinate with the activist fund. Such a compensation scheme could also have to be disclosed in the company's annual report as well as potentially calling into question the director's independence under applicable corporate governance codes.

Mandatory bids

13 Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

In France, where a person, acting alone or in concert, comes to hold directly or indirectly more than 30 per cent of a company's equity securities or voting rights, such a person is required, on its own initiative, to inform the AMF immediately and to file a proposed offer for all the company's equity securities, as well as any securities giving the right to acquire its share capital or voting rights, on terms that have to be acceptable to the AMF. The same obligations apply to persons, acting alone or in concert, who directly or indirectly hold between 30 per cent and 50 per cent of the total number of equity securities or voting rights of a company and who, within a period of less than 12 consecutive months, increase such holding by at least 1 per cent. Exceptions and waivers to the obligation to file a proposed offer may apply in both cases.

Under French law, persons are deemed to act in concert if they enter into an agreement with a view to acquiring, selling or exercising voting rights, in order to implement a policy with respect to a company or to obtain control of the company. Circumstantial evidence tending to show a tacit or hidden agreement may be taken into account in assessing the existence of such an agreement.

Disclosure rules

14 Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

In accordance with primary disclosure obligations in France, any person acting alone or in concert with others that comes to hold more than 5, 10, 15, 20, 25, 30, 33 and a third, 50, 66 and two-thirds, 90 or 95 per cent of the share capital or voting rights in a publicly listed company is required to report the crossing of these ownership thresholds (in either direction) to the company and the AMF no later than the close of market on the fourth trading day following the date on which the threshold was crossed. In addition, persons holding temporary interests in 2 per cent or more of the voting rights in a publicly listed company must notify the issuer and the AMF of these holdings no less than three business days prior to any shareholders' meeting at which those rights may be exercised.

More generally, persons preparing a financial transaction that may have a significant impact on the market price of public securities must disclose the transaction to the public as soon as possible.

The disclosure obligations also require that any holder that comes to hold 10, 15, 20 or 25 per cent of the share capital or voting rights of an issuer report to the AMF its intentions for the next six months with respect to the issuer and its shareholding, no later than the close of market on the fifth trading day following the crossing of the relevant threshold. To the extent any such statement of intentions becomes inaccurate, the holder in question is required to rapidly communicate its new intentions.

In addition to the legal thresholds, the company's articles of incorporation may provide that shareholders must inform the AMF and the company of the crossing of additional ownership thresholds below 5 per cent in increments of no less than 0.5 per cent.

Any agreement that provides preferential rights with respect to the sale or purchase of shares representing at least 0.5 per cent of the share capital or voting rights of a publicly listed company must be reported to the AMF within five trading days of its signature.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

As indicated above, the disclosure requirements apply to persons acting alone or in concert. In addition, for the purposes of calculating the thresholds described above, the 'share capital or voting rights' include, in addition to ordinary share holdings, all derivative products entitling the reporting person at its sole option to acquire existing shares (or corresponding voting rights) and cash-settled or physically-settled derivative instruments providing an economic exposure equivalent to a long position in the underlying shares. The disclosure obligations also require that net short positions in shares be reported to the AMF upon crossing the threshold of 0.2 per cent of issued share capital (and every 0.1 per cent above that), and disclosed to the public when they reach 0.5 per cent of issued share capital (and every 0.1 per cent above that).

Insider trading

16 | Do insider trading rules apply to activist activity?

Activists can be, and have been, found guilty in France of insider trading.

Under French rules, insider trading consists of using 'privileged' information by acquiring or selling, or attempting to acquire or sell financial instruments to which that information relates. 'Privileged' information is defined under French law as any information of a precise nature that has not been made public and that, if it were made public, would be likely to have a significant effect on the price of the relevant financial instruments or on the prices of related financial instruments. The AMF considers information to be precise when such information is sufficiently detailed and complete to permit the information to be used by an investor as the basis for an investment decision.

It should be emphasised that the information need not be 'inside' information, and that there is accordingly no need under French law to demonstrate the violation of any duty, whether in relation to the company or some third party.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

As previously discussed, a defining duty of directors in France is to act in accordance with the corporate interest of the company.

There is no different standard applicable to activist proposals.

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

Appropriate planning for an activist attack includes laying the groundwork for strong teamwork in a crisis by and among the board, management and advisers as well as other key internal constituencies. Maintaining strong relationships and lines of communication with external constituencies, notably including significant shareholders, is essential.

Companies should engage in ongoing monitoring and be ready to respond to early warning signs, particularly during vulnerable periods (eg, active M&A operation under way, results or other metrics remain below those of peers, enduring criticism of governance or leadership, etc). Continuously assessing corporate strategy to ensure that it is rigorously defensible becomes paramount in the event that the business underperforms compared with peers. Maintaining good governance, and a relationship of trust with regulators, are also worthwhile investments.

Shareholder activism and engagement has been a subject of increasing focus in French boardrooms in recent years, with a significant uptick in awareness in the past 12 months.

Defences

19 | What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

In the event an activist does emerge, a strong response by the company often includes rallying the company's financial, legal and communications advisers at short notice and making sure that any public communications by the company are coherent and disciplined across all key constituencies. The board and management should redouble efforts to maintain strong cohesion. Individualised outreach may be appropriate to key shareholders. In addition, ongoing monitoring should be maintained to ensure the company can rapidly respond to any additional tag-along attacks or related activity. An open line of communication should typically be maintained with the relevant authorities such as the AMF, as well as proxy advisers and other key constituencies, including other significant shareholders. Given the likely heightened focus on the company and its conduct during the time of the attack, a particular effort should be made to avoid legal or other missteps that will be seized upon by the activist or others (including the AMF). Likewise, the activist's actions and statements should be carefully reviewed for missteps or weaknesses in its strategy. In certain cases, seeking regulatory intervention or even initiating litigation against the activist may be appropriate.

Proxy votes

20 | Do companies receive daily or periodic reports of proxy votes during the voting period?

In France, the record date for shareholder voting is legally set at two trading days prior to the meeting. Many companies listed in Paris outsource their share registrar (including the management of voting at shareholders' meetings) to external service providers. These service providers may keep issuers apprised of the general tendency of votes received as from the date of the initial notice of the meeting but, in any event, the bulk of the voting returns are not available until the last few days preceding the shareholders' meeting.

As background, French public companies must provide their proxy voting guidelines in a notice that must be made at least 35 days prior to the meeting. Shareholders must be provided with a supplemental notice of meeting no less than 15 days prior to the meeting. Both notices must specify, among other details, the deadline for the return of proxy forms.

Shareholders may choose between one of the three following options of participation:

- attend the general meeting in person;
- grant proxy to the chairman of the shareholder's meeting or to any individual or legal entity of their choice or;
- vote by post (or electronically if permitted).

Under the relevant legislation, the proxy forms must be provided by mail to the company at least three days prior to the meeting, except if a shorter period is permitted under the company's bylaws, or if to be provided electronically, the proxy forms must be received by the company no later than 3pm on the day prior to the meeting.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

Formal settlements with activists are relatively rare; however, there are precedents, including Valeo and Saint Gobain. It may be necessary to disclose the main terms of such agreements under AMF rules.

These agreements may include board representation, an undertaking not to vote in favour of resolutions that do not have board approval, a cap on voting rights or a standstill and pre-emption rights.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

Companies may adopt a variety of different organised shareholder engagement efforts including communication via the company website, shareholder newsletters, shareholder guides, shareholder clubs, consultative committees, meetings with shareholders and educational outreach, and preferred dividends and loyalty shares.

23 Are directors commonly involved in shareholder engagement efforts?

Promoting direct dialogue between directors and shareholders has been a subject of increased focus in France, notably in response to growing pressure from institutional investors. In this respect, the AFEP-MEDEF governance code (as applied by the majority of the CAC 40) was amended in June 2018 and introduced the concept of the chairman of the board of directors, or a 'lead' director, being entrusted with shareholder relations, in particular with regard to corporate governance, although other subjects are not excluded.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Subject to certain exceptions, French law imposes on issuers an ongoing obligation to disclose any inside information directly concerning the issuer as soon as possible. The issuer is responsible for ensuring the effective and complete disclosure of the inside information; among other things, this requires that the issuer promptly post such information on its website. Thus, for example, in the event that non-public information is inadvertently shared with the activist, that information must generally be promptly disclosed to the market.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

Under French law, shareholders are permitted to solicit proxies from other shareholders, with limited requirements and restrictions as compared to other jurisdictions. In this respect, any person who actively solicits proxies must present its voting policy on its website. Such a person may also publicise its intentions as to any draft resolutions that may be before the shareholders, in which case the person soliciting proxies is required to vote consistently with the intentions that it has publicised. A person who represents others at a shareholder meeting may also under certain circumstances be subject to other disclosure requirements.

Proxy solicitation may lead to a risk of acting in concert with other shareholders who come to share the activist's views, which may be the case either in the context of true proxy solicitation or in the context of more general efforts to persuade and coordinate with other shareholders. In addition, it is a criminal offence to agree to any payment or other benefit in exchange for voting or abstaining from voting at a shareholders' meeting.

As part of the shareholder engagement efforts described above, management is in a position to communicate its views on the best direction for the company. In addition, the draft resolutions provided to shareholders in the notice of meeting will typically include the board of directors' recommendations on how shareholders should vote for each resolution.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

Any shareholder may request a list of the nominal shareholders (including the number of shares held) as of the date 16 days prior to the shareholders' meeting from the company at any time during the 15 days that precede the meeting. Shareholders may also request at any time the shareholder attendance sheets for the shareholders' meetings of the prior three years. However, only the company may seek out the identity of the ultimate beneficial shareholders, and even the company may only do so in the event that its bylaws specifically so provide. In any event, as discussed above, beneficial shareholders holding in excess of 5 per cent of the share capital or voting rights are required to disclose this (and various other thresholds) to the company and the AMF, and the AMF provides these disclosures to the public on its website.

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

Notable recent activist campaigns includes TCI's acquisition of a 4 per cent stake in Safran following Safran's announcement of its intention to acquire Zodiac Aerospace in 2017. TCI sought the cancelation of the takeover based on its view that the price was too high and that the structure of the transaction would effectively disenfranchise Safran shareholders. TCI publicly lobbied the AMF to intervene, threatened Safran board members with litigation and sought to add a resolution regarding the transaction to the agenda of Safran's annual meeting. Following significant underperformance by Zodiac, a revised, lower, transaction price was announced. 90 per cent of Safran shareholders voted in support of the revised offer.

More recently, Elliott Management disclosed a stake in Pernod Ricard and has made public calls for the company to launch a new operational improvement plan and improve its corporate governance.

If current conditions and trends continue, activism appears poised to continue to play a vibrant role in France. Based on worldwide trends, we may expect a maturing of the international component of French activism, including:

- more major activist interventions in France;
- non-activist institutional becoming more 'active', ranging from supporting activists campaigns (Financière de l'Echiquier in its team-up with Sterling Strategic Value concerning Latécoère) to themselves opportunistically going activist (eg, occasional activist PSAM in its Vivendi campaign);
- companies becoming the targets of distinct serial activist interventions (in addition to wolf packs); and
- more sophisticated and increasingly M&A focused activist campaigns.

We may also see an increase in activism against targets that had previously been sheltered by the French state as the French state reduces its exposure in certain listed companies. In addition, as activism becomes commodified, an increase in local activism may occur, as a new generation of smaller European and French players join the fray. It remains to be seen whether Elliott Management's victory in Telecom Italia may encourage activists to become more aggressive vis-à-vis companies with reference shareholders that lack outright control (a shareholder structure that is relatively common in Europe), or whether that matter will remain an outlier based on its very specific circumstances.

DARROIS VILLEY MAILLOT BROCHIER

Bertrand Cardi
bcardi@darroisvilley.com

Forrest G Alogna
falogna@darroisvilley.com

69 Avenue Victor Hugo
75116 Paris
France
Tel: +33 1 45 02 19 19
Fax: +33 1 45 02 49 59
www.darroisvilley.com

Germany

Martin Schockenhoff, Gabriele Roßkopf and Martin Hitzer
Gleiss Lutz

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The primary source of law relating to shareholder activism and engagement is the German Stock Corporation Act (AktG), including the unwritten principle of shareholders' duty of loyalty with respect to the company's and the other shareholders' legitimate interests. Provisions applying only to listed companies (ie, companies the shares of which are admitted to stock exchange trading on regulated markets; section 3(2) AktG) and their shareholders can be found in particular in the EU Market Abuse Regulation (Regulation No. 596/2014/EU, including various accompanying level 2 and level 3 acts), the EU Regulation on Short Selling (Regulation No. 236/2012/EU), the German Securities Trading Act (WpHG) and the German Securities Acquisition and Takeover Act (WpÜG). The primary sources of laws and regulations relevant for listed companies are either directly applicable EU regulations or are based on EU directives that aim to fully harmonise the capital market laws in all EU member states, such as the EU Transparency Directive (Directive 2013/50/EU amending Directive 2004/109/EC), the EU Market Abuse Directive (Directive 2014/57/EU) and the Shareholders' Rights Directive (Directive (EU) 2017/828 amending Directive 2007/36/EC). Accordingly, the relevant German federal laws, which are acts of parliament, are partially based on EU directives (also see 'Update and trends' for upcoming legislation).

Shareholders can enforce their rights generally in front of the civil courts. The breach of specific obligations of the management (concerning, for example, the truthfulness of certain declarations and reports or information provided in shareholders' meetings) can be prosecuted as a statutory offence (section 399 et seq, AktG). Regulations concerning listed companies are enforced by the competent supervisory body (ie, the Federal Financial Supervisory Authority (BaFin)).

Certain industries (eg, banking and insurance) are subject to additional regulations that are supervised and enforced by BaFin or certain EU institutions, in particular the European Securities and Markets Authority (ESMA).

In addition to statutory law as described, the German Corporate Governance Code (DCGK) contains recommendations and suggestions based on internationally acknowledged standards for the best practice of corporate governance. The aim is to support a more transparent and comprehensible corporate governance system in order to enhance the confidence of investors, clients, employees and the general public in German listed companies. The DCGK is not mandatory, but deviations have to be explained and disclosed in an annual declaration of conformity, which has to be published on the company website, section 162, AktG (see 'Updates and trends').

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

The number of activist campaigns has risen continually over recent years. Their chances of succeeding depend largely on whether the claims appear likely to increase the value of the shares. The chances of success hinge especially on whether the activists uncover unknown weaknesses or potentials of the company or receive support from proxy advisers and institutional investors.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

Initially, the management and large shareholders in German companies as well as the general public were in general sceptical about activist shareholders. More recently, this perception has changed and became more differentiated, depending on the approach and the quality of the proposals of the activist shareholders.

There is a clear tendency that the boards of large listed companies are interested in a dialogue with activist shareholders who make constructive proposals or who can be expected to gain substantial support from other shareholders. Activist shareholders can expect support from other shareholders, provided these can benefit from the initiative taken by the activist shareholders as well and further provided the initiative is reasonable with regard to the companies' best interests. A rising number of initiatives taken by activist shareholders is aligned with ongoing public discussions about, inter alia, potential corporate governance issues, allegedly poor strategic planning or voluminous management remuneration plans and bonus payments.

Shareholder activism appears across all industries. The following prominent companies have been targeted by activists' campaigns in the past:

- Adidas (sports and lifestyle);
- Bilfinger (construction);
- Celesio (pharmaceuticals);
- CeWe Color (digital media);
- Conergy (solar power);
- Demag Cranes (engineering);
- Deutsche Bank (finance)
- Deutsche Börse (stock exchange);
- Deutsche Telekom (telecommunications);
- E.ON (energy);
- Gildemeister/DMG Mori (engineering);
- Hochtief (construction);
- Hypo Vereinsbank (finance);
- Infineon (semiconductors);

- IWKA (engineering);
- Kabel Deutschland Holding (cable provider);
- KUKA (engineering);
- Porsche Automobil Holding (car manufacturing);
- Röhn Klinikum (health);
- SLM Solutions (engineering);
- STADA Arzneimittel (pharmaceuticals);
- Ströer (digital media, advertisement);
- ThyssenKrupp (steel, engineering);
- Uniper (energy);
- Volkswagen (car manufacturing); and
- Wirecard (digital financial services).

To date, there is no legislation underway dealing specifically with shareholder activism. However, BaFin recently issued a general prohibition on establishing and increasing net short positions in shares of Wirecard based on article 20 of EU Regulation No. 236/2012. This was explicitly supported by ESMA.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

Shareholder activists not only exercise their statutory rights as shareholders, but try to leverage their influence beyond their proportionate shareholding through informal measures (eg, letters to the management, public campaigns, etc). In the public awareness, mainly hedge funds have been viewed as activist shareholders. However, this has changed recently. Some investment funds or private equity investors have acquired substantial holdings and publicly adopted a medium term or long-term strategy. In several cases, representatives of activist shareholders have acquired seats in the supervisory board of their respective target company. Activist shareholders can expect support from other shareholders, provided these can benefit too, and the proposals are reasonable with regard to the company.

Activist shareholders in this sense must be discerned from (i) shareholders trying to make a short-term profit from well prepared short sale attacks and (ii) notorious claimants who make use of statutory minority rights in order to block resolutions on structural measures adopted by the majority. Contrary to notorious claimants, activist shareholders are strongly interested in their proposals being implemented.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

Shareholder activism mainly focuses on the following topics:
- corporate strategy and restructuring measures (eg, Bilfinger and ThyssenKrupp);
- takeover bids (eg, Uniper, Deutsche Börse, Gildemeister, Kabel Deutschland Holding, Celesio and SLM Solutions);
- corporate governance, in particular changes in composition of management or supervisory board (eg, Infineon, KUKA, STADA and Volkswagen);
- return of value to shareholders (eg, ThyssenKrupp);
- short sale attacks (eg, Wirecard and Ströer);
- debt-for-equity swaps (eg, Conergy); and
- damages claims in Germany and in other jurisdictions (eg, Porsche Automobil Holding and Volkswagen).

Activist shareholders in Germany do not focus on sociopolitical activism (environmental, political, ethical, or gender discrimination). There are small non-profit organisations with typically very small shareholdings that use shareholders' meetings as a platform to bring forward their views on these topics. Other factors that attract the attention of shareholder activists are:
- a high free float (in particular because of traditionally low attendance of free float at shareholders' meetings in Germany);
- a specific capital structure, for example, significant cash positions or defensive financial gearing or strong cash generation opportunities not being utilised;
- an unsatisfactory share price performance or a vague business strategy, which leads to poor business prospects;
- a conglomerate structure; and
- takeover and restructuring situations.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

It is becoming increasingly common that activist shareholders apply pressure and vigorously pursue change in their respective 'target' company. When doing so, activist shareholders regularly seek to gain mainstream investor support.

Strategies based on minority shareholder rights

Most activist strategies are based on statutory minority shareholder rights, which, to some extent, depend on a minimum amount of capital stock held by the respective activists.

Basic minority rights are granted to each shareholder, regardless of the number of shares he or she owns. All shareholders are entitled to, for example:
- attend and speak at a shareholders' meeting;
- make counterproposals before or at a shareholders' meeting (section 126, AktG);
- request information at a shareholders' meeting. Every shareholder is entitled to ask questions in the shareholders' meeting (section 131(1), AktG) and request information that has been disclosed to other shareholders (section 131(4), AktG);
- use the shareholders' forum in the Federal Gazette (section 127a, AktG);
- commence litigation against shareholders' resolutions (section 245 Nos. 1–3, AktG);
- pursue damages claims against controlling shareholders or against management or supervisory board members (section 309(4) and sections 317(4) and 318(4), AktG); and
- request the appointment of a supervisory board member by the court to fill a vacancy (section 104(1), AktG).

Other minority rights depend on the amount of capital stock the shareholders are holding. For example, shareholders holding:
- 1 per cent of the capital stock or €0.1 million nominal share value may:
  - request a special audit by a court-appointed auditor (section 142(2), AktG); or
  - request the permission of the court to pursue liability claims against members of the management or supervisory board (section 148, AktG);
- 5 per cent of the capital stock or €0.5 million nominal share value may:
  - request amendments to the agenda of a shareholders' meeting (section 122(2) No. 1, AktG). For example, a resolution to change the corporate charter, remove supervisory board members or pursue liability claims against the management or supervisory board members; or

    - request the permission of the court to make amendments to the agenda public (section 122(2), (3), AktG);
- 5 per cent of the capital stock may:
    - request the company to call a shareholders' meeting (section 122(1) No. 1 AktG); or
    - request the permission of the court to call a shareholders' meeting (section 122(2), (3) AktG);
- more than 5 per cent of the capital stock may block a squeeze-out of minority shareholders (section 327a, AktG);
- 10 per cent of the capital stock or €1 million nominal share value may:
    - request an individual vote on dismissal of management or supervisory board members (section 120(1), AktG); or
    - request a court-appointed representative to pursue liability claims against members of the management or supervisory board (section 147(2), AktG);
- 10 per cent of the capital stock (or less if capital stock is not fully represented in the shareholders' meeting) may nominate members of the supervisory board in a privileged way (section 137 AktG);
- more than 10 per cent of the capital stock may block a merger-related squeeze-out of minority shareholders (section 62(5), UmwG); and
- more than 25 per cent of the capital stock (or less if capital stock is not fully represented in the shareholders' meeting) may block amendments of the corporate charter and other major shareholder resolutions – for example, capital increases, corporate agreements, or transfer of substantially all of the company's assets (sections 179(2) and 179a(1) AktG).

Strategies based on majority shareholder rights

Those who hold majority shareholder rights may:

- initiate a vote of no confidence with respect to management board members (a simple majority at the shareholders' meeting; section 84(2), (3), AktG); or
- remove members of the supervisory board (a three-quarters majority at the shareholders' meeting; section 103(1), AktG).

Informal strategies

Informal activism is less common, although there are various informal strategies that activists may use to pursue their objectives. For example:

- a letter to the management or supervisory board;
- a request to meet the management or members of the supervisory board, in particular its chairman;
- public campaigns to encourage shareholders to vote in a certain way;
- publishing white papers or research reports;
- proxy solicitation;
- utilising proxy advisers who provide research, advice and recommendations on how to vote in shareholders' meetings;
- fast or hidden stakebuilding; and
- short-selling, sometimes after having published critical reports on the target company.

Processes and guidelines

7 | What are the general processes and guidelines for shareholders' proposals?

Shareholders' proposals concerning items of the agenda of a shareholders' meeting (counter proposals)

At shareholders' meetings, every shareholder is entitled to speak, to ask questions (section 131, AktG) and to make proposals directed against proposals of the management or the supervisory board under specific items of the agenda (section 126, AktG). Shareholders are not required to notify the company in advance of such proposals, but if the company receives such a proposal including the shareholder's name and the reasons for the proposal in writing at least 14 days before the relevant meeting, the proposal (including shareholder's name and reasons) must be made accessible to other shareholders as well as to certain institutions and persons mentioned in section 125(1)–(3), AktG. This usually means that such proposals are published on the company website. For listed companies, publication on the company website is mandatory (section 126(1), AktG). The company does not have to make proposals accessible only in exceptional circumstances (such as section 126(2), AktG). If several shareholders present proposals in respect of the same subject, the management board may combine such proposals and respective statements of the reasons (section 126(3), AktG), without curtailing or corrupting the proposals.

Shareholders' proposals concerning other subjects

Shareholders' proposals concerning subjects other than items on the agenda are only admissible if the agenda is amended accordingly. Only shareholders individually or collectively holding shares representing at least 5 per cent or €0.5 million nominal share value (or less if stated in the corporate charter) of the company's capital stock may request that additional items be placed on the agenda of a shareholders' meeting (section 122(2), AktG). Requests, including the reasons or a draft resolution, must be addressed to the company's management board in writing and must be received by the company at least 24 days (in case of non-listed companies) or 30 days (in case of listed companies) prior to the shareholders' meeting. Requesting shareholders must prove that they have held the sufficient number of shares (quorum) for the legally required minimum period of ownership of 90 days, which has to be calculated from the date of receipt by the company.

As long as shareholders comply with the formal requirements, there are very few reasons why a company may reject such request; for example, if the request is directed at a resolution that would be unlawful, or if the request constitutes an abuse of shareholder rights or conflicts with the shareholder's duty of loyalty.

Amendments to the agenda of non-listed companies must be made public in the Federal Gazette (or by registered mail to all shareholders if they are known to the company and the corporate charter does not stipulate differently; section 121(4) AktG), either upon calling the meeting or immediately following receipt of the request. Listed companies must publish amendments to the agenda on their website (section 124a, AktG) and, if the company has issued bearer shares, forward the information to the media (section 121(4a), AktG).

If the company does not comply with such request, relevant shareholders may apply to the competent court (ie, the local court at the registered seat of the company) for authorisation to amend the agenda and to publish such amendment accordingly at the company's cost (sections 122(3) and (4), AktG).

Common shareholders' proposals

Naturally, the type of shareholders' proposals depends on the company involved and the individual situation at hand, but common subjects are:

- counterproposals regarding profit distribution;
- proposals of supervisory board candidates;
- the appointment of special auditors (sections 119(1) No. 7 and 142, AktG);
- the enforcement of certain compensation claims against board members or other persons; and
- the appointment of special representatives to enforce these claims (section 147, AktG).

Mandatory voting rights

The shareholders' meeting is competent only as far as expressly provided for by corporate law or by the corporate charter. The following examples are particularly relevant:

- amendments of the corporate charter (sections 119(1) No. 5 and 179(1), AktG);
- appointment and removal of members of the supervisory board, as far as they are not appointed under the co-determination regime (sections 119(1) No. 1 and 103(1), AktG);
- allocation of distributable profits (section 119(1) No. 2, AktG);
- approval of the actions of the members of the management and supervisory board (section 119(1) No. 3, AktG);
- appointment of the company auditor (section 119(1) No. 4 AktG);
- capital increase or reduction (section 119(1) No. 6, AktG);
- management matters put before the shareholders' meeting by the management (section 119(2), AktG);
- decisions of major importance for the company such as major divestments or drop-downs (based on (controversial) case law known as the Holzmüller-Gelatine doctrine);
- appointment of special auditors (sections 119(1) No. 7 and 142, AktG);
- enforcement of certain compensation claims against board members or other persons (section 147(1) AktG) and appointment of special representatives to enforce these claims (section 147(2), AktG);
- liquidation of the company (sections 119 (1) No. 8 and 262 No. 2, AktG) as well as the continuation of a liquidated company (section 274, AktG);
- transfer of substantially all of the company's assets (section 179a(1), AktG);
- issuing convertible, warrant or dividend bonds as well as participation rights (section 221 AktG);
- affiliation agreements (section 293(1),(2) AktG);
- integration of one stock corporation into another (section 319 AktG);
- squeeze-out (section 327a AktG); and
- restructuring measures (changes of the legal form, mergers, demergers under the Merger and Reorganisation Act (UmwG)).

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

All shareholders are entitled to make proposals for the election of supervisory board members. Proposals do not need to include reasons, but should contain name, occupation and domicile of the proposing person. If a proper proposal is received by the company in writing at least 14 days before the relevant meeting, it must be made available to other shareholders (or the public) on the company website (see question 7).

Shareholders cannot make proposals for members of the management board as they are appointed by the supervisory board, usually following a selection process conducted by the chairman of the supervisory board to find suitable candidates.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Request to call a shareholders' meeting

Shareholders who together hold at least 5 per cent of the capital stock (or less if stated in the corporate charter) may require the company to call a shareholders' meeting (section 122(1), AktG). The request should be addressed to the management board in writing and state the objective and reasons. Requesting shareholders must prove that they have held a sufficient number of shares (quorum) for the legally required minimum period of ownership of 90 days, such period being calculated from the date on which the company received the request.

Permission to call a shareholders' meeting at the company's expense

If the company fails to comply with a proper request to call a shareholders' meeting, the requesting shareholders may apply to the competent court (ie, the local court at the registered seat of the company) for authorisation to call a shareholders' meeting at the company's expense (section 122(3), (4), AktG).

Exercise of voting rights

Shareholders are entitled to exercise their voting rights in shareholders' meetings. They may not act by written consent without a meeting. However, there are various options for voting in a meeting:

- proxy voting (sections 134(3) and 135, AktG); and
- postal vote (section 118(2), AktG) or online participation (section 118(1), AktG), if the corporate charter provides for such way of voting.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Main types of litigation

Shareholders can initiate lawsuits relating to their membership rights, particularly the right to attend the general meeting (section 118(1), AktG), to request a general meeting or to request amendments to the agenda of a general meeting (section 122, AktG), to obtain information (section 131, AktG) or to receive dividends (sections 58(4), 60, AktG). Shareholders can also bring actions against the company to challenge shareholder resolutions adopted by the general meeting: In case of severe breaches listed in section 249, AktG, shareholders may bring an action for the declaration of nullity, or in other cases to set aside the resolution (section 246, AktG). If compensation is offered to shareholders with regard to certain structural measures such as squeeze-outs, mergers, profit and loss transfer agreements and so on, shareholders can request the adequacy of the compensation offered to be examined by the court in special proceedings regulated by the Appraisal Proceeding Act (SpruchG).

Individual shareholders are generally not entitled to assert claims against members of the board of management or the supervisory board that neglect their duties. In principle, such claims have to be raised by the supervisory board against members of the management board and vice versa (sections 93 and 116, AktG). They can in theory also be raised by shareholders but only in the name of the company after approval by the court (section 148, AktG) and to the effect that payment is to be made to the company.

Derivative actions

Shareholders who together hold at least 1 per cent of the capital stock or an amount of €0.1 million nominal share value may request that the court allows them to pursue liability claims on behalf of the company against members of the management or supervisory board (section 148, AktG).

Class actions

German law does not provide for class actions. However, depending on the subject matter, model case proceedings are available under the Capital Investors Model Proceedings Act and the General Model Proceedings Act.

Methods of obtaining access to company information

The Stock Corporation Act does not grant shareholders full access to company information – they do not have a right to review the company's books and records. However, shareholders have a right to request information from the management board in the annual general meeting to the extent that such information is necessary for an appropriate evaluation of an agenda item (section 131(1), AktG). This includes information about the legal and business relationships between the company and an affiliate. The management board may refuse access to information in certain instances (section 131(3), AktG). If access to information is refused, shareholders may initiate court proceedings to enforce the right to information (section 132, AktG), challenge majorly shareholders' resolutions (sections 241 et seq, AktG) or motion to appoint special auditors (section 142, AktG).

SHAREHOLDERS' DUTIES

Fiduciary duties

11 | Do shareholder activists owe fiduciary duties to the company?

Each shareholder owes a general duty of loyalty to the company and to other shareholders. The duty of loyalty is based on case law and imposes limits on the power of the majority as well as on minority rights.

Shareholders who influence members of the management or supervisory board to act against the interests of the company may be held liable for damages (section 117, AktG). Furthermore, German corporate law concerning groups of companies provides that a controlling shareholder (who has not entered into a domination agreement) is obliged to refrain from any act that is disadvantageous for the controlled company unless the disadvantage is compensated in cash at the end of the respective business year. Controlling shareholders may be held liable for uncompensated disadvantages (section 317, AktG).

Compensation

12 | May directors accept compensation from shareholders who appoint them?

Members of the supervisory board are elected by the shareholders, and members of the management board are appointed by the supervisory board.

Members of the supervisory board are usually compensated by the company. However, they may accept direct compensation from shareholders under certain circumstances.

Whatever the case, members of the supervisory board are not allowed to accept compensation from shareholders if conflicts of interest arise. All duties of the supervisory board are primarily owed to the company (and not the shareholders), regardless of whether a member receives direct compensation from shareholders or not. Members of the supervisory board who are in breach of their duties may be held liable under civil and criminal law. In principle, members of the management board may not accept any compensation from third parties (eg, shareholders) owing to statutory restraints on competition.

Mandatory bids

13 | Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

Acting in concert requires joint conduct of shareholders in the form of an agreement or by other means:

- in respect of the exercise of their voting rights; or
- with the objective of permanently and substantially changing the company's business strategy (section 34(2), WpHG; 30(2), WpÜG).

The respective voting rights of parties acting in concert are attributed to each other. If, together, they hold at least 30 per cent of the voting rights, they are deemed to be in control of the company (section 29 (2), WpÜG). In this case, the shareholders are obliged to disclose their proportion of the voting rights within seven days (section 35(1) WpÜG). In addition, within four weeks of disclosure, they must submit a mandatory bid (section 35(2) WpÜG).

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Listed companies

Shareholdings in listed companies (see question 1) must be disclosed if the voting interest in the company (directly or indirectly by way of attribution) reaches, exceeds or falls below 3, 5, 10, 15, 20, 25, 30, 50 or 75 per cent (sections 33 and 34, WpHG). In this case, shareholders must notify the company and BaFin without undue delay (within four trading days at the latest).

Furthermore, shareholders whose voting rights exceed 10 per cent are required to inform the company within 20 trading days (section 43, WpHG):

- of the aims they pursue with the investment;
- whether they plan to acquire further voting rights within the next 12 months, to exert influence on the management's composition or to seek changes of the capital structure, including the company's dividend policy; and
- of the origin of the funds used for the investment.

Voting rights from shares held by subsidiaries are deemed equivalent to voting rights from shares held directly by the parent company (section 34(1), WpHG).

Shareholders must notify the commercial register if they have acquired all shares of the company (section 42, AktG).

Disclosure of derivative holdings

Positions in instruments (eg, transferable securities, options, forward purchases, swaps, interest adjustment options, contracts for difference) through which voting shares can be acquired or in instruments that have a similar economic effect are subject to the same disclosure requirements as shares, except for the minimum threshold for a disclosure being 5 per cent instead of 3 per cent (section 38, WpHG). A netting between short and long positions resulting from derivatives is not permitted. For the purpose of determining whether a threshold has been reached, voting rights from shares and instruments are aggregated (section 39, WpHG).

Acting in concert

Disclosure requirements also apply to shareholders acting in concert. The voting rights of parties that act in concert are attributed to each

other (see question 13 for when shareholders are deemed to be acting in concert).

Sanctions for non-compliance

Failure to comply with disclosure requirements may lead to the loss of certain shareholder rights (section 44(1), WpHG). In case of wilfully or grossly negligent misconduct, the right to dividends will be lost.

Shareholders could be fined up to €2 million for non-compliance by BaFin. If the shareholder is a legal entity, the maximum fine rises (according to whichever is the highest) to:

- €10 million;
- 5 per cent of the legal entity's revenue in the past fiscal year; or
- up to three times the legal entity's economic advantage (profits made or losses avoided owing to misconduct).

Furthermore, offences will be made public on the internet by BaFin ('naming and shaming').

Non-listed companies

Shareholders of non-listed companies are subject to disclosure rules if they are enterprises. The term 'enterprise' covers all types of corporations and partnerships. Individuals may, under certain conditions, be deemed enterprises as defined by the AktG.

If an enterprise or a subsidiary of an enterprise holds (directly or indirectly by way of attribution) more than 25 per cent of the shares of a stock corporation (section 20 (1), AktG) or a majority of the shares (section 20 (4), AktG), it is required to promptly inform the stock corporation of this in writing. The stock corporation must also be informed if the holding of an enterprise falls below the level requiring disclosure. For the purpose of determining whether a threshold has been reached, shares already held by the enterprise or its subsidiaries and shares whose transfer may be required, or shares that the enterprise or its subsidiaries are obligated to acquire, will be aggregated (section 20(2), AktG).

In case of non-compliance with the disclosure requirements, rights arising from shares may not be exercised (section 20(7), AktG).

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

See question 14.

Insider trading

16 | Do insider trading rules apply to activist activity?

Listed companies are subject to restrictions on insider trading and more general market abuse rules (eg, under the EU Market Abuse Regulation), which further restrict selective disclosure of non-public information to shareholders. Furthermore, the mere fact that information has been disclosed to an activist shareholder could qualify as inside information.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

In general, directors are obliged to enable all shareholders to exercise their rights in a proper and unimpeded manner. Shareholder activists and other shareholders must be treated equally. Board decisions regarding activist proposals are subject to the same standard of care as other board decisions.

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

As a general measure, companies should identify potential vulnerabilities by analysing their business and strategy as an activist shareholder would do.

Following such analysis and risk-assessment, the following defence measures should be considered:

- preparing investor or public relations statements;
- implementing a 'one voice policy';
- appointing a rapid reaction team; and
- analysing the shareholder structure and other 'early warning signs' on a regular basis.

Shareholder activism has increased significantly in recent years in Germany. According to Lazard, in 2018, there were 58 campaigns of activist investors targeting listed companies in Europe, a significant number hereof being directed at targets in Germany.

Defences

19 | What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Available structural defences are:

- the existence of majority shareholders;
- preference shares (non-voting shares);
- restricted transferability of registered shares;
- staggered terms of members of the supervisory board; and
- delisting.

Other factors that make a company more likely to be targeted are:

- a high free float (traditionally low attendance of free float at shareholders' meetings);
- a specific capital structure, eg, significant cash positions or defensive financial gearing or strong cash generation opportunities not being utilised;
- an unsatisfactory share price performance or a vague business strategy that leads to poor business prospects;
- a conglomerate structure; and
- takeover and restructuring situations.

New rules on delisting from regulated markets require that an unconditional tender offer be made to all shareholders (section 39, BörsG). This will result in a more complex and costly delisting process and presumably limit the role of delisting as a defence mechanism against activist shareholders.

Based on the new Shareholders' Rights Directive, companies will be entitled to identify their shareholders and to obtain information regarding shareholder identity from any intermediary in the chain that holds the information. The purpose is to facilitate the exercise of shareholder rights and their engagement with the company. The member states may provide that companies are only allowed to request identification with respect to shareholders holding more than a certain percentage of shares or voting rights that will not exceed 0.5 per cent.

The new requirements aim to increase transparency and help the companies in their approach to shareholder engagement. Institutional

investors and asset managers will either have to develop and publicly disclose a policy on shareholder engagement or explain why they have chosen not to do so.

Owing to the important influence on voting behaviour of investors, proxy advisers will also be subject to transparency requirements (eg, disclosure of methods and main sources of information) and a code of conduct.

Details remain to be seen since national implementation is not due before 10 June 2019.

Proxy votes

20 | Do companies receive daily or periodic reports of proxy votes during the voting period?

There is no statutory proxy voting system outside the shareholders' meeting. The corporate charter may provide that shareholders vote in writing or by way of electronic communication. However, a vote made in such a way becomes binding only at the beginning of the voting procedure in the shareholders' meeting. Until then, any vote made in writing or by electronic communication may be rescinded by the shareholder.

In practice, votes cast outside the shareholders' meeting are kept confidential, and there is no exchange between management and shareholders on votes submitted before the shareholders' meeting.

Settlements

21 | Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

Private settlements with activists are not explicitly prohibited. However, any settlement with activists has to be in the best interest of the company, comply with the principle of equal treatment of shareholders (section 53a, AktG) and may not lead to a repayment of capital other than distributable profits (section 57, AktG). As a consequence, any private settlements that lead to an economic advantage for activists holding at least one share has to be published and benefit the other shareholders equally. Private settlements can, as the case may be, bring about inside information that is subject to the mandatory rules on the disclosure of inside information.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 | Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

With a view to the general legal obligations (i) to treat all shareholders equally in principle and to grant all shareholders access to the same information and (ii) to keep the company's affairs confidential and to not disseminate inside information, German listed companies in the past usually abstained from organised shareholder engagement efforts outside of the reporting obligations imposed by law and regulation. Exceptions have always been normal investor relation efforts such as regular analysts' conferences, meetings, calls and such like. However, listed companies in Germany have recently begun to put a stronger focus on communication with specific groups of shareholders or even a single shareholder. Such engagement can be legally permissible provided that such 'exclusive' communication is in the best interests of the company and not only in the interests of the respective shareholders. The question if and to what extent a listed company may (or may not) engage with an activist shareholder very much depends on the individual case at hand and requires a careful analysis of all circumstances, in particular regarding the goals of the activist shareholder and the situation of the company. As a rule of thumb, the management board of the company will be more inclined (or even obliged) to engage in direct communication with an activist shareholder if the approach is well structured and presented in a way that can be viewed as being beneficial not only to the activist shareholder, but to the long-term interests of the company and its stakeholders as well.

23 | Are directors commonly involved in shareholder engagement efforts?

Save for very few exceptions, German listed companies are represented as regards third parties, including its shareholders, exclusively by the management board (section 78, AktG). Therefore, if a company chooses to engage directly with activist shareholders, it is common practice that a managing director (often the CFO and, in important cases, also the CEO) is involved. Less common but increasing in number are cases in which the chairman of the supervisory board is involved in direct communication with activist shareholders. In light of the management board's exclusive right to run the business and operations of the company (section 76(1), AktG), the chairman of the supervisory board may only discuss, subject to the general legal restrictions set out under question 22, those topics with activist shareholders that are within the competence of the supervisory board – for example, the composition of the management board or its remuneration. In order to make the dialogue between institutional investors and supervisory boards as fruitful as possible, the initiative 'Developing Shareholder Communication' has formulated eight guiding principles that are addressed to investors and listed companies in Germany with a supervisory board. Direct communication between the investor and the supervisory board can create added value for both parties. Such a dialogue allows investors to get first-hand information on whether the supervisory board is properly staffed and works effectively. In turn, the supervisory board has the opportunity to explain to foreign investors the German two-tier system and the national characteristics of co-determination.

Disclosure

24 | Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Companies are not required to publicly disclose their shareholder engagement efforts.

Generally, selective or unequal disclosure of non-public information is not permitted. If a shareholder has received information from the management board outside a shareholders' meeting, such information shall, upon request, be provided to any other shareholder (section 131 (4), AktG). However, selective disclosure on the basis of non-disclosure agreements is permitted if in line with the interests of the company (eg, due diligence in a friendly takeover scenario).

Listed companies are subject to restrictions on insider dealing and more general market abuse rules (eg, under the EU Market Abuse Regulation), which further restrict selective disclosure of non-public information to shareholders. Furthermore, the mere fact that information has been disclosed to an activist shareholder could qualify as inside information.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

AktG does not require a special system for direct communication between the company and its shareholders. The majority of the communication takes place at the general meeting. As most listed companies have issued registered shares, they know the name and addresses of each shareholder, which enables them to send them serial or individual messages if so required in specific cases.

Rules relating to selective disclosure of non-public information to shareholders are detailed in question 24.

Communication can be conducted by companies via:

- website;
- Federal Gazette;
- letter;
- email; and
- social media.

Communication can be conducted by activist shareholders via:

- the press;
- social media; and
- shareholders' forum in the Federal Gazette (section 127a, AktG).

Companies may offer shareholders to authorise proxy agents appointed by the company (section 134 (3), AktG). However, according to the prevailing opinion, the authorisation of a company proxy to vote at a shareholders' meeting requires that detailed voting instructions are given by the shareholder.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

Stock corporations do not need to maintain a register of known holders of bearer shares.

Stock corporations with registered shares have to maintain a share register, but are not permitted to make the register available to the public or to other shareholders owing to privacy requirements (data protection legislation). Shareholders may only request information relating to their own shareholding. Hence, requests to provide a list of other registered shareholders by an activist shareholder can easily be (and in most cases should be) resisted. Recently, there have been efforts to entitle companies to have their shareholders identified and to allow further processing of the information in the share register in order to facilitate the exercise of shareholder rights and engagement with the company.

However, each shareholder has the right to be, upon request, granted access to the list of participants of a shareholders' meeting for review until up to two years after the meeting (section 129 (4,) AktG). The list of participants states name and place of residence (in the case of par shares), the amount (in the case of non-par shares), the number and the class of shares represented by each person present at the meeting.

Gleiss Lutz

Martin Schockenhoff
martin.schockenhoff@gleisslutz.com

Gabriele Roßkopf
gabriele.rosskopf@gleisslutz.com

Martin Hitzer
martin.hitzer@gleisslutz.com

Lautenschlagerstrasse 21
70173 Stuttgart
Germany
Tel: +49 711 8997 0
Fax: +49 711 855096
www.gleisslutz.com

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

The EU shareholder rights directive ((EU) 2017/828) has to be transposed into German law until 10 June 2019.

New features to be implemented are:

- the right for listed companies to have their shareholders identified and to directly communicate with them;
- new public disclosure requirements for institutional investors and asset managers (investment strategies and engagement policies, certain aspects of arrangements with asset managers, and votes cast);
- a code of conduct for proxy advisers;
- a binding or advisory vote on the remuneration policy; and
- control of related-party transactions.

The German Corporate Governance Code is currently under review. A draft of the new version was published in late 2018 and was widely discussed (www.dcgk.de/en/consultations/current-consultations.html). The draft preamble focuses on institutional investors and calls them to exercise their right of ownership in an active and responsible manner.

The draft DCGK further intends to increase the public acceptance of executive compensation by making it more comprehensible. Another important change will be the definition of requirements for the independence of supervisory board members.

Hong Kong

Sherman Yan and Dominic Wai
ONC Lawyers

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The primary source of laws and regulations are the Companies Ordinance (Cap 622) (Companies Ordinance). Given that listed companies are involved, the Securities and Futures Ordinance (SFO), the Main Board Listing Rules and the GEM Board Listing Rules, and the Codes on Takeovers and Mergers and Share Buy-backs (Takeovers Code) also apply. (Unless otherwise specified, 'Listing Rules' refers to the Main Board Listing Rules).

The current version of the Companies Ordinance was passed by the Hong Kong Legislative Council on 12 July 2012 and came into force on 3 March 2014. Sections 732 and 724 of the Companies Ordinance are particularly relevant to shareholder activism and engagement and apply to both Hong Kong companies and non-Hong Kong companies (defined as a company incorporated outside Hong Kong that has established a place of business in Hong Kong).

The SFO was enacted by the Legislative Council on 13 March 2002 and came into force on 1 April 2003. Part 15 of the SFO, which sets out the laws relating to disclosure of interest (beneficial ownership in the company), is particularly relevant to shareholder activism.

The Listing Rules and the Takeovers Code are made and enacted by the Hong Kong Exchanges and Clearing Limited (HKEx) and the Securities and Futures Commission (SFC) respectively. The Listing Rules are administered and enforced by the Stock Exchange of Hong Kong Limited (Exchange) primarily and the SFC. The Takeovers Code is regulated by the Takeovers Panel, a committee of the SFC.

The Listing Rules apply to matters related to those securities and issuers with securities listed on the Hong Kong stock market whereas the Takeovers Code applies to takeovers offers, merger transactions and share buy-backs affecting public companies in Hong Kong.

The legislations relating to shareholder activism and engagement are supplemented by the Corporate Governance Code and Corporate Governance Report (CG Code) set out in Appendix 14 of the Listing Rules. The provisions in the CG Code are not mandatory rules and deviations from the provisions are acceptable if listed companies consider there are more suitable ways for it to comply with the principles of the CG Code. Nevertheless, listed companies are expected to comply with the CG Code and must state whether they have complied with the CG Code and the reasons for non-compliance (if any) in their interim reports and annual reports. This is commonly described as the 'comply or explain' approach.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Despite an increasing prevalence of activist campaigns, there is no sufficient data to deduce the frequency of the activist campaigns in Hong Kong and the chance of success of the campaigns. To date, the successful activist campaigns in Hong Kong known to the public include the campaign instituted by Passport Special Opportunities Master Fund (Passport) to prohibit a listed company, eSun Holdings, from proceeding with its private placement.

On the contrary, BlackRock Inc failed to block G-Resources Group Limited from selling its crown-jewel gold mine at near book value. PAG Limited's campaign to buy Spring REIT also failed since it only obtained support from 41.5 per cent of Spring REIT's shareholders, falling below the required threshold of 50 per cent.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

Companies controlled by families or the Chinese government (known as state-owned enterprises) are a predominant form of listed companies in Hong Kong. As such, less protection has been accorded to minority shareholders and these companies are hostile to outsiders including shareholder activists generally. Nevertheless, there is continuing growth in shareholder activism and awareness of minority shareholders' protection over the past few years in Hong Kong. More long-term shareholders and institutional investors have become increasingly concerned about the operation and governance of their investee companies. They are of the view that ownership of shares shall be accompanied by the right to speak and vote on matters that may affect how a business is run. In this regard, the SFC also published 'Principles of responsible Ownership' (Principles) in March 2016, which sets out how investors may meet their ownership responsibilities, such as reporting to the listed company its policies for discharging ownership, monitoring their investee companies, and establishing clear policies on when they will escalate their engagement activities. Despite its non-binding and voluntary nature, the Principles will serve the purpose of promoting corporate governance for the protection of shareholders' interest and improving the performance of the investee company and the Hong Kong financial market in the long run.

On 27 July 2018, the HKEx published the 'Guidance for Boards and Directors' detailing the roles and responsibilities of the directors with a view to promoting good corporate governance among listed corporations.

Also in July 2018, the Exchange tightened the Listing Rules on capital-raising activities by listed issuers that create unfairness to the

minority shareholders. Following the amendments, all open offers require prior approval from the minority shareholder unless the shares are issued under an existing general mandate.

Shareholder activism seems to have become more widespread in all industries. Some companies that have recently been subject to a public activist campaign includes, Bank of East Asia (BEA); G-Resources (a mining company); China Motor Bus (CMS), a property developer; and Spring REIT (a real estate investment trust). There is no traceable pattern showing that the activists are targeting a specific industry. It is anticipated that shareholder activism will become a feature of the corporate landscape in Hong Kong.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

In Hong Kong, the shareholder activists instituting campaign publicly are mainly institutional shareholders and short-seller activists.

Institutional shareholders, which are mainly asset management companies focusing on long-term investment, often put pressure on the corporation to achieve corporate governance change, including but not limited to BlackRock, Argyle Street Management Limited and Passport. With a view to successfully launching an activist campaign, institutional investors will normally identify and align with other minority shareholders and hedge funds. Hedge fund activists may also institute a campaign by themselves such as Elliott Management Corporation.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

The focus of shareholder activism in Hong Kong is making demands in relation to major strategic transactions of the company, which is normally triggered by the underperformance of the corporation or a transaction that will unfairly prejudice the interest of minority shareholders. For instance, Elliott and Passport raised an activist campaign to oppose a placement agreement proposed by the investee listed company, whereas minority shareholders of Power Asset Holdings Limited raised an activist campaign to oppose the proposed merger with Power Asset raised by Cheung Kong Infrastructure Holdings Limited. Recently, in 2018, BlackRock also urged the minority shareholders of G-Resources to vote against the company's sale of a gold mine at an undervalue since the sale price is unreasonably low and such proposal will completely alter the nature of business of G-Resources. The reason behind these shareholder activist campaigns are the prejudicial effects caused by the management's proposal to the minority shareholders' interest.

Another focus of shareholder activism is a demand for a higher shareholder yield. On 19 October 2016, David Webb, a well-known shareholder activist in Hong Kong, told Ming Fai International Holdings to distribute a special dividend out of the proceeds of a proposed asset disposal through publishing an open letter. H Partners Management LLC also demanded that Hong Kong Economic Times Holdings Ltd (HKET) distribute a special dividend through open letters published on newspaper dated 11 July 2011. In 2017, Argyle Street urged the board of CMS to distribute more dividends since the stocks had been undervalued.

Operational demand, such as a demand for a change to board composition and management structure, is less common in Hong Kong. For instance, the Children's Investment Fund Management (UK) LLP published various newspaper articles announcing its demand to remove the chairman of Link REIT in 2006. The relatively small number of operational demand in Hong Kong is probably due to the lack of the requirement of minimum board representation for minority shareholders in Hong Kong. Besides, almost all listed companies in Hong Kong only issue one class of shares and each share carries equal voting right.

Nevertheless, listed companies have now been allowed to issue dual-class shares since April 2018. It remains to be seen whether more operational demand will be raised by activists.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

The common strategies adopted by the activists may be divided into three non-mutually exclusive categories, namely informal strategies, voting strategies and legal strategies.

Informal strategies comprise private engagement, public announcement, open letters or publications, and website campaign, with private engagement being the most common and preferred form. Preliminarily, activists will enter into a private dialogue and attend meetings with the company management to pursue their objectives and press for a change. Thereafter, activists may write to other shareholders detailing their proposals and persuade them to vote in favour of the proposals or resolution in private.

In the case of private negotiation break-down, activists may resort to public intervention. The activists may make a public announcement and publish an open letter stating their demand in order to draw the public's attention and exert pressure on the controlling shareholders. H Partners Management LLC wrote a public letter to HKET seeking support from other shareholders to vote in favour of its proposal for distributing special dividends. The letter was published in various newspapers on 11 July 2011. Publications are also another tactic adopted by shareholder activists such as BlackRock. BlackRock published 'Corporate governance and proxy voting guidelines for Hong Kong securities' in January 2019, in which it details its engagement approach, its expectation of the company improving its corporate governance, and voting policies.

Shareholders activists will also institute website campaign and publish their demands against the company, such as:-

- David Webb's demands against various listed corporations (https://webb-site.com/);
- Elliott's demand against BEA (https://fairdealforbea.com/); and
- Argyle Asset's open letters to CMB (https://unlockvaluecmb.com/author/brianlwh/).

Nevertheless, shareholder activists generally would not resort to website campaigns or public announcements unless there is sufficient evidence to substantiate a reasonably articulable suspicion.

Besides informal strategies, shareholder activists will also avail the voting rights accorded to them under the Listing Rules and the Takeovers Code. For instance, Cheung Kong, a shareholder holding 38.87 per cent stake in Power Asset, proposed to merge with Power Asset. However, 49.23 per cent of the independent minority shareholders exercised their veto right and successfully opposed the proposed merger.

If the activists do not receive a positive response after utilising the informal strategies, they may escalate their engagement activity and employ legal tactics, for instance, applying for an inspection order and an injunction order to exert pressure on the company and the management. Pursuant to section 740 of the Companies Ordinance, a shareholder holding at least 2.5 per cent of the voting rights at the general meeting or five shareholders collectively may apply to the court for an order inspecting any record or document of the company. The court shall satisfy itself that the inspection is for a proper purpose and in good faith before granting an inspection order. Nevertheless, an inspection order may be an essential but not effective legal strategy as

shown in the Elliott's campaign against the private placement proposed by BEA. Elliott applied for an inspection order for documents relating to the private placement. Within one month after the application for an inspection order and before the grant of such order, the private placement was approved. Nevertheless, Elliott launched an action against the BEA upon inspecting and obtaining the documents relating to the private placement. As of the publication date, the litigation between Elliott and the BEA is still ongoing.

An injunction order, as compared with an inspection order, would be a more effective and preferable legal tactics in the eyes of activists. Passport instituted a campaign against the private placement by eSun and applied for an ex parte injunction order to prohibit eSun from proceeding with the private placement. The application succeeded and the proposed placement agreement was eventually terminated.

Besides interim legal measures, activists may also commence legal proceedings against the company, such as an unfair prejudice claim, shareholder derivative actions (see question 10) and a winding-up petition. Interim measures aside, Passport and Elliott also filed an unfair prejudice claim with a view to terminating the placement agreement and releasing the shareholders from the obligation under the private placement agreement respectively.

Under section 724(1) of the Companies Ordinance, a shareholder of the company, including a non-Hong Kong company, may also bring an unfair prejudice action if the affairs of the company are being or have been conducted in a manner that is unfairly prejudicial to the interest of the members in general or one or more members. Another basis for a shareholder to bring the action is an actual or proposed act or omission of the company that is or would be prejudicial.

According to the Honourable Mr Justice Fuad in *Re Taiwa Land Investment Co Ltd* [1981] HKLR297, 'unfairly prejudicial' means the conduct departing from accepted standards of fair play that amounts to unfair discrimination against the minority. The conduct complained of must be both unfair and prejudicial.

Examples of unfair prejudicial conduct include:

- a breach of the Companies Ordinance (such as failure to obtain members' approval for non-pro rata allotment of shares: *Re a company* (No. 005134 of 1986), *ex p Harries* [1989] BCLC 383);
- a breach of the Listing Rules (for instance, the minority shareholders' effort in blocking the resolution to amend the articles of association of a listed company when the provisions therein contravened the Listing Rules: *Luck Continent Ltd v Cheng Chee Tock Theodore* [2013] 4 HKLRD 181);
- a breach of shareholders agreement (*Re Bondwood Development Ltd* [1990] 1 HKLR 200);
- a breach of fiduciary duties (such as misappropriation of company assets: *Re Tai Lap Investment Co Ltd* [1999] 1 HKLRD 384); and
- a long-term policy of not paying dividends, or paying low dividends without commercial reasons (*Choi Chi Wai v Cheng Ka Shing* [2017] HKEC 850).

The remedies for a successful unfair prejudice claim include:

- an order restraining the continuance of the unfair prejudicial conduct of the company (section 725(2)(a)(i) of the Companies Ordinance);
- an order regulating the conduct of the company's affairs in future (section 725(2)(a)(iv)(A) of the Companies Ordinance);
- an order to purchase the shares of any member of the company by the company or another member of the company (sections 725(2)(a)(iv)(A) and 725(2)(a)(iv)(B) of the Companies Ordinance);
- an order to pay damages by the company or any other person (section 725(2)(b) of the Companies Ordinance);
- appointment of receiver or manager (section 725(3) of the Companies Ordinance);
- an order for alteration of a company's articles (*Roberts v Walter Developments Pty Ltd* (No.2) (1992) 10 ACLC 804); and
- any other orders the court thinks fit (section 725(2)(a)(iv)(D) of the Companies Ordinance).

Further, or in the alternative, to an unfair prejudice claim, shareholders may also apply for a winding-up of a Hong Kong company on just and equitable grounds pursuant to section 177(1)(f) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Companies Ordinance (Winding up)). A winding-up order of foreign companies, including non-Hong Kong companies, on just and equitable grounds shall be sought under section 327(3)(c) of the Companies Ordinance (Winding up). The SFC may also wind up a listed company under section 212 of the SFO to protect the company's minority shareholders if it is in the public interest to do so; namely, the winding-up order is in line with the objectives and functions of the SFC as set out in sections 4 and 5 of the SFO. For instance, in *Re China Metal Recycling (Holdings) Ltd* [2015] 2 HKLRD 747, the respondent company, which had disseminated fraudulent information in its prospectus, was ordered to be wound up upon the SFC's application in 2015.

Examples of just and equitable grounds include:

- the mutual breakdown of trust and confidence (*Re Yung Kee Holdings Ltd* (2015) 18 HKCFAR 501, in which there is a breach of common understanding that two sons of the original controller of the company shall operate the company together); and
- frustration of the company's objects (*Re Mediavision Ltd* [1993] 2 HKC 629, in which there is final and conclusive abandonment of the original business of the company).

Nevertheless, it should be noted that the winding-up application shall not be made as a matter of course where there is also an unfair prejudice claim made by the shareholders (*Re Sun Light Elastic Ltd* [2013] 5 HKLRD 1). Shareholders must specify why a winding-up order is an appropriate relief for the unfair prejudice claim.

It is also worth noting that the above case laws relating to unfair prejudice and winding up on just and equitable grounds largely concern private limited companies. Although, as a matter of general principle, they shall be equally applicable to listed companies, the fact that a listed corporation may have a large number of shareholders involved and the fact that the corporation is also subject to the regulation of the HKEx may introduce a certain degree of uncertainty as to the extent to which these principles are applicable to listed corporations.

For instance, while a breach of the Companies Ordinance may be considered as an unfairly prejudicial conduct, a mere breach of the Listing Rules by a listed company would not automatically give rise to unfair prejudice (*Re Astec (BSR) plc* [1998] 2 BCLC 556). However, in the context of a listed company (as opposed to a private company), it was held that there was a common understanding among the shareholders that the company should maintain its listing status and therefore, actions jeopardising the listing status of the company could amount to unfair prejudice (*Luck Continent Ltd v Cheng Chee Tock Theodore* [2013] 4 HKLRD 181). Nonetheless, according to *Re Blue Arrow plc* [1987] 3 BCC 618 (Ch), any breach of any informal understanding that is said to supplement a listed company's articles of association is unlikely to be regarded as an unfair prejudice since the investing public is entitled to assume that the company's articles are full and complete and there is no private agreement reached in relation to the articles.

Regardless of which strategies shareholder activists have adopted, they will increase their stakes in the company simultaneously to exert further pressure on the investee companies. Should the campaign raised by the activists fail, they will usually sell its stake in the company in order to minimise its loss.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

First, shareholders should identify the nature of subject matter of their demand; namely, whether they are demanding distribution of dividends, a change to board composition and governance structure, a change to the business model or termination of a proposed transaction.

Shareholders should familiarise themselves with the requirement for convening a general meeting. Pursuant to section 566 of the Companies Ordinance, 5 per cent of the total voting rights of all members having a right to vote at general meetings can request the board of directors to hold a general meeting and such a request should be made in hard copy form or electronic form. The content of the request shall specify the general nature of the business to be dealt with at the meeting and may include the text of a resolution intended to be moved at the meeting.

Directors must convene a general meeting within 21 days upon receipt of the request and the meeting must take place within 28 days of the notice convening the meeting pursuant to section 567 of the Companies Ordinance. If the directors fail to do so, the members who requested for the general meeting, or any of them representing more than half of the voting rights of all of them, may themselves convene a meeting at the company's expense according to section 568(1) of the Companies Ordinance.

Annual general meetings (AGM) shall instead be convened by directors. In default, shareholders of the company may apply to the court for an order calling an AGM according to section 610(7) of the Companies Ordinance. Unlike extraordinary general meetings (EGM), there is no provision for a specified number of shareholders to requisition an AGM.

Notice of general meetings shall be sent by the company to its shareholders in hardcopy or electronic form. The length of notice for AGMs and EGMs are 21 clear days and 14 clear days respectively according to section 571 of the Companies Ordinance. Subject to the provisions in the articles of association, the length of notice is the same regardless of whether the resolutions to be passed in the AGM are ordinary or special.

If shareholders are unclear about the procedure to nominate a candidate for election as a director, they may refer to the procedures published by the subject Hong Kong listed company on its website. The listed company will be in contravention of Rule 13.51D of the Listing Rule if it fails to do so.

Shareholders should satisfy the threshold required for passing their proposed resolution (namely, ordinary resolution or special resolution), which is normally stated in the Companies Ordinance and the company's articles of association. Each company is free to draft its own customised set of articles and set a different threshold for different resolutions. Assuming the investee company follows the Model Articles of Association for public companies limited by shares (Model Articles), the following subject matters could only be resolved by a special resolution (namely, a majority of at least 75 per cent):

- directions by the shareholders to take or refrain from doing certain acts (articles 3 and 4 of the Model Articles);
- reduction of share capital (section 226(1) of the Companies Ordinance); and
- alteration of object clause (section 89 of the Companies Ordinance).

On the contrary, some subject matters could be resolved by an ordinary resolution (namely, a majority of at least 50 per cent), such as the appointment of director (article 23 of the Model Articles).

If shareholders' demands relate to distribution of dividends, regardless of interim or final, shareholders shall be bound by the maximum limit of the amount of dividends recommended by the directors according to article 91 of the Model Articles.

If shareholders challenge certain transactions proposed by the company or the majority shareholders, they should identify whether the proposed transaction is subject to shareholders' approval. Pursuant to the Listing Rules, certain transactions require approval from shareholder such as:

- connected transaction (Rules 14A.03 and 4A.36);
- major acquisition or disposal transaction (Rules 14.33(2), 14.40 and 14.44);
- very substantial acquisition or disposal transaction (Rules 14.33(2), 14.44 and 14.49); and
- reverse takeovers (Rules 14.33(2), 14.44 and 14.55).

Furthermore, certain transactions specifically required the approval of minority shareholders according to the Listing Rules, such as:

- right issues or open offers (Rules 7.19A(1) and 7.27A); and
- open offers (Rules 7.24A(1) and 7.27A).

It is noteworthy that, according to Rules 2.15 and 14.33 of the Listing Rule, when a transaction or arrangement proposed by the listed company is subject to shareholders' approval, shareholders having a material interest and his or her close associate must abstain from voting.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Shareholders are entitled to nominate a candidate to stand for election as a director. Assuming the company adopts the Model Article, shareholders may require a shareholder meeting to be convened or a resolution to appoint a director to be tabled at the meeting in accordance with the procedure set out in question 6. If the director fails to convene a general meeting, a shareholder may do so at the company's expense. Moreover, according to article 24(10) of the Model Articles, a shareholder shall send the company a notice of his or her intention to propose the person to be appointed as a director and that person shall also send the company a notice of his or her to be appointed at least seven days before the general meeting.

According to Rule 13.70 of the Listing Rules, if a notice is received from a shareholder's proposal for nominating directors for election after the publication of the Notice of Meeting, the listed company shall publish an announcement or issue a supplementary circular, in which particulars of the proposed director shall be included.

Shareholders representing at least 2.5 per cent of the total voting rights or at least 50 members who have a right to vote at the general meetings are empowered to request for:

- circulation of the resolution proposed by them for the AGM at the company's expense provided that such request is sent to the company not later than six weeks before the AGM or the time at which notice of that meeting is given (sections 615 and 616 of the Companies Ordinance); and
- circulation of statement relating to a matter mentioned in a proposed resolution and other business to be dealt with at the general meetings (sections 580 and 581 of the Companies Ordinance).

The costs of circulation of statement on extraordinary general meetings shall be governed by the company's article. In the absence of such provisions in the articles, members who made the request for circulation shall bear the expenses (section 582 of the Companies Ordinance). On the contrary, the cost for the circulation of statement in relation to an AGM shall be borne by the company if such a request is received by the company in time so that the company could send a copy of the

same together with the notice of the general meeting (section 582 of the Companies Ordinance).

If shareholders are unclear about the procedure to nominate a candidate for election as a director, they may refer to the procedures published by the subject Hong Kong listed company on its website. Rule 13.51D of the Listing Rules obliges all listed companies to publish the procedures.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

In Hong Kong, special general meeting of the shareholders is also known as extraordinary general meeting or special shareholders' meeting. Regarding Hong Kong incorporated companies, 5 per cent of the total voting rights of all the members having a right to vote at the general meeting have a statutory right to request an extraordinary general meeting according to section 566 of the Companies Ordinance (see question 6).

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

The main types of litigation shareholders may institute against corporations and directors are statutory derivative actions and claims for unfair prejudice.

Shareholders have a statutory right to bring a derivative action for and on behalf of a Hong Kong company, a non-Hong Kong company and an associated company of the company, in respect of a misconduct committed against the corporation according to sections 731 and 732 of the Companies Ordinance. It was, however, not appropriate for an individual shareholder to take a derivative action if he or she had a personal grievance against the company and if the wrong complained of was not done to the company.

Misconduct is defined as 'fraud, negligence, breach of duty, or default in compliance with any Ordinance or rule of law' under section 731 of the Companies Ordinance. The usual reasons for bringing a derivative action are:

- fraudulent, oppressive or ultra vires act (*Anglo-Eastern (1985) Ltd v Karl Knutz* [1988] 1 HKLR 322, [1987] 3 HKC 80, CA);
- acts not authorised by the company's articles (section 116(3) of the Companies Ordinance);
- criminal act (*Cockburn v Newbridge Sanitary Steam Laundry Co Ltd and Llewellyn* [1915] 1 IR 237);
- majority of the votes being controlled by wrongdoers control (*Smith v Croft* (No 2) [1988] Ch 114, [1987] 3 All ER 909); and
- resolution not passed by the required threshold (*Baillie v Oriental Telephone and Electric Co Ltd* [1915] 1 Ch503)

Prior to bringing a statutory derivative action, shareholders should first obtain leave from court and the court will consider the following factors stated in section 733 of the Companies Ordinance before making a decision:

- whether the proposed action appears to be in the company's interests;
- whether there is a serious question to be tried and the company has not itself brought the proceedings;
- whether the member has served written notice on the company 14 days prior to the application for leave; and
- whether the plaintiff has already commenced any common law derivative action on the same subject matter.

Shareholders also have a common law right to bring a multiple derivative action on behalf of the corporation in respect of the wrongdoer's fraudulent act according to *Waddington Limited v Chan Chun Hoo Thomas and others* (2008) 11 HKCFAR 370. While the statutory derivative action does not displace the right to bring a common law derivative action, two derivatives action are mutually exclusive. Nowadays, in Hong Kong, statutory derivative action is more prevalent in use.

The possible defences to derivative actions are first, the nature of the subject act is not a 'misconduct' for the purpose of section 732 of the Companies Ordinance. The company may also raise the plaintiff's conducts as a defence thereto if such conduct would make it inequitable for it to bring such an action. The company may also rebut the derivative actions on the ground that they are acting properly within their powers.

The remedies of statutory derivative action are set out in sections 737(1)(2) of the Companies Ordinance, which include:

- an interim order pending the determination of the derivative action
- an order directing the company or its officer to provide or not to provide information, or to do or not to do any act; and
- an order appointing an independent person to conduct investigation and report to the court.

Shareholders cannot commence class actions on behalf of all shareholders since there is no class action regime in Hong Kong at this juncture. Nevertheless, the SFC has indicated in the Consultation Conclusions on the Principles of Responsible Ownership published in March 2016 that it will consider the introduction of class action rights in the future and when appropriate.

Shareholders can gain access to company information online free of charge. Rule 13.90 of the Listing Rules requires the listed companies to publish their announcements and their up-to-date bylaws on the Exchange's website (www3.hkexnews.hk/listedco/listconews/advancedsearch/search_active_main.aspx) and its own website.

In addition to the online public information and as discussed in question 6, shareholders holding at least 2.5 per cent of the voting rights at the general meeting or five shareholders collectively are entitled to apply to the court to inspect any record or document of the company pursuant to section 740 of the Companies Ordinance. Moreover, under section 631 of the Companies Ordinance, shareholders may make a request for inspection of Register of Members free of charge and for inspection of any other register, index, agreement, minutes or other documents that a company is required to keep, such as Register of Charges, upon the payment of HK$50 as an inspection fee.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

Shareholders in Hong Kong, regardless of whether they are a majority, minority or significant shareholder, do not owe a fiduciary duty to the company. Instead, the directors owe a fiduciary duty to the company.

Compensation

12 | May directors accept compensation from shareholders who appoint them?

Directors shall not accept direct compensation from shareholders who nominate them if there is a conflict of interest. Directors owe a fiduciary duty to the company and must act in good faith in the interests of the company as a whole. A director also must not make any secret profits in relation to his or her fiduciary capacity to the company. Accepting such direct compensation is likely to be regarded as a breach of fiduciary duty. Upon the finding of a breach of fiduciary duty, the court may order a wide range of remedies including an injunction, damages and the contract being void or voidable, according to sections 728(4) and 729 of the Companies Ordinance.

Moreover, according to sections B.1.2 and B.1.2(c) of the CG Code, no director should be involved in deciding his or her own remuneration. A director's salary shall be determined by the remuneration committee. It is therefore unlikely that the directors shall accept direct compensation from shareholders who nominate them.

Mandatory bids

13 | Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

'Acting in concert' is defined under the Takeovers Code as 'persons who, pursuant to an agreement or understanding (whether formal or informal), co-operate, to obtain or consolidate control of a company or to frustrate the successful outcome of an offer for a company'. Unless the contrary is established, certain classes of persons or corporations are presumed to be acting in concert with others in the same class, including but not limited to its parent company, its subsidiaries, its directors, and its financial or professional advisers. The Takeovers Panel will consider all circumstances when deciding whether parties are acting in concert.

While activists may solicit support from other minority shareholders of the company on a particular resolution, for instance, a change to board composition, such act will not generally render activists acting in concert with other minority shareholders. This is because Rule 26 Note 4 of the Takeovers Code explicitly provides that shareholders voting together on a particular resolution would not lead to an offer obligation although that circumstance may be taken into account as one indication that the shareholders are acting in concert.

The mandatory bid requirement is contained in Rule 26 of the Takeovers Code, which provides that a person and his or her concerted parties acquiring 30 per cent or more voting rights of a company is required to make a general offer to all shareholders of the company unless a waiver is granted. Any additional purchase of 2 per cent voting rights shall also be subject to mandatory offer obligation.

Nevertheless, according to Rule 26.2 of the Takeovers Code, a mandatory offer must be conditioned on the offeror receiving more than 50 per cent of the voting rights. If the offeror holds more than 50 per cent of the voting rights before the general offer is made, such offer made thereunder must normally be unconditional.

According to Rule 8.3 of the Takeovers Code, the mandatory general offer document must contain information required by Schedule I to the Takeovers Code, particularly the details of the identity of any concert parties, the interests in securities held by the offeror in the target company, together with any other information that will enable shareholders of the target company to make an informed decision.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Shareholders in Hong Kong must disclose significant shareholdings. Persons holding 5 per cent or more interest in a Hong Kong listed company shall notify the Exchange and the subject listed company pursuant to sections 310(1), 311, 313 and 315 of the SFO. An initial notification shall be made within three business days after the date of acquiring 5 per cent or more voting rights or the date when such person was aware of its occurrence (whichever is later). If voting share capital held by such person falls below 5 per cent or increases, subsequent notifications shall be made within 10 days after its occurrence.

To comply with the duty of disclosure, shareholders must complete and submit the Disclosure of Interest forms (DI forms) to the Exchange through the Disclosure of Interest Online System (DION System). Notification by hand, post, fax or email is longer accepted. The DI forms can be downloaded at the Exchange news website.

After receiving the notification from the shareholders, the listed company shall record such interest in the shares and the name of the shareholder in the register pursuant to section 336 of the SFO.

If a shareholder fails to make a disclosure within the time limit stipulated in the SFO or makes a false or misleading statement, he or she shall be penalised and may subject to a maximum fine of HK$100,000 or a maximum prison sentence of two years for each offence pursuant to section 328 of the SFO.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

Disclosure obligations in Part 15 of the SFO do apply to 'equity derivatives' according to section 311 of the SFO. According to section 308 of the SFO, 'equity derivatives' include various derivative instruments, such as rights, options and warrants.

Under section 312 of the SFO, short positions shall be disclosed in accordance with section 310 of the SFO.

Sections 336 and 352 of the SFO require all the listed companies to keep a register of interests in shares and short positions, and a register of directors' and chief executives' interests and short positions respectively. See question 14.

Disclosure obligations in Part 15 of the SFO also apply to persons acting in concert. According to section 317 of the SFO, when two or more persons who are a party to an agreement to acquire 5 per cent or more interests in a listed company will be required to disclose such interest and submit the relevant documentation.

Insider trading

16 | Do insider trading rules apply to activist activity?

Insider dealing rules and the SFO do apply to activist activity. Please refer to the last paragraph of question 24 below.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

The fiduciary duties of directors have been discussed in question 12. In particular, when considering all resolutions and proposals tabled in

front of directors (whether they are an activist proposal or not), directors must act in good faith in the interest of the company, exercise their powers for proper purposes, must not enter into ultra vires transactions, and shall avoid conflict of interest.

It is not mandatory for directors to consider an activist proposal. The standard for considering an activist proposal is the same as other board decisions, namely reasonable care, skill and diligence (section 465 of the Companies Ordinance and Rule 3.08 of the Listing Rules). 'Reasonable care, skill and diligence' means the general knowledge and experience that is actually possessed by the director and that may reasonably be expected of a person carrying out the director's functions.

Preparation

18 What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

It is strongly suggested that the company shall follow the CG Code, in particular sections D.3 and E, in order to minimise the risk of facing shareholder activism.

A company may routinely review its shareholder engagement policy and regularly solicit feedbacks from shareholders on its corporate strategy and governance. A corporate governance guideline setting out the routes for the shareholders to provide feedbacks on its business operation could also be published for the sake of clarity.

A company may also enhance its transparency in its corporate decisions and management structure by publishing the guidelines or code of business conduct that it follows. As such, the activists will gain access to more information as to the company's decision-making process and will take these information into account prior to instituting an activist campaign.

Regular strategic reviews should also be conducted. A company should regularly evaluate and compare its performance, cost structure, revenues, management structure and the independence and expertise of its directors, with its counterparts in order to discourage activist campaigns because of its underperformance.

Unusual trading of its stock shall also be closely monitored since the larger stakes held by shareholders, the more likely that they will become a shareholder activist and exercise their minority veto rights.

Companies should be open-minded towards an activist's proposal and step into the shoes of an activist. A unilateral decision to ignore an activist may provoke the activist to start a campaign. An individual committee could be formed to analyse the activist's proposal.

Nevertheless, the above are only general principles that a company may follow and shall be subject to the factual situation in each case.

Defences

19 What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Some jurisdictions allow dual-class shareholding structures, in which a particular class of share shall carry more voting rights than another. While Hong Kong also allows listed applicants with a weighted voting right structure that satisfy the requirements stated in Rule 8A.06 in the Listing Rules to apply for listing, the companies that have already listed in Hong Kong are not allowed to adopt a weighted voting right structure at this juncture according to Rule 8A.05 of the Listing Rules.

Certain procedural safeguards are already in place for the company. Assuming the company has adopted the Model Articles, under article 2 therein, the business and affairs of the company are managed by the directors (but not shareholders), who may exercise all powers of the company. Rule 3.08 of the Listing Rules also reflects the rule that it is the board, not the shareholders, who shall be responsible for the management and the operation of the company. Hong Kong courts shall intervene only when the boundaries of discretion are transgressed.

If shareholders would like to reallocate the power between general meeting and the board, they may take preventives measure to amend the articles of the company. When customising its own articles, companies may or may not grant powers to the directors subject to the control of the shareholders via a decision achieved by a certain level of majority (eg, by an ordinary resolution). Nevertheless, the alteration of the articles of Association shall not be made unfairly prejudicial to the minority or in contravention of the Companies Ordinance. Each case is fact-sensitive and whether the alteration amounts to an unfair prejudice depends on the nature and degree of the benefit to the company.

It should be noted that the resolution to alter its articles shall only be passed by special resolution. As such, companies shall take prompt actions before activists together with its alliance accumulate a total shareholding of 25 per cent.

However, even if the resolution to amend the articles is blocked by a minority shareholder holding more than 25 per cent interest, the majority shareholder may bring a claim for unfair prejudice if the articles violate the provisions in the Listing Rules. For instance, in *Luck Continent Ltd v Cheng Chee Tock Theodore* [2012] HKEC 567, the majority shareholder of Luck Continent Ltd successfully applied to the court for an order of amending the articles based on an unfair prejudice claim. This is because the articles of association require a special resolution for the removal of director, which is in contravention of the threshold stated in the Listing Rules, namely ordinary resolution, but the minority shareholder repeatedly exercised his or her minority veto right to block the resolution for alteration of such provisions in the article.

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

A proxy form offering two-way voting on all resolutions must be sent together with the Notice of General Meeting to its shareholders and must be submitted for publication on the Exchange's website according to Rule 13.38 of the Listing Rules. The time and place for lodging proxy forms shall be stated in the proxy form. It is a common practice in Hong Kong that shareholders shall lodge proxy forms at the share registrar of a listed company. As such, whether the companies receive daily or periodic reports of proxy votes during the voting period depends on the common practice of different share registrars in Hong Kong and the agreement entered into between the listed company and its share registrar.

Nevertheless, the SFC imposes an obligation on all share registrars to ensure all communications between the listed company and its registered shareholders that the share registrar is instructed to distribute are distributed in a timely, accurate and appropriate manner in accordance with paragraph 5.5 of the Code of Conduct for Share Registrars.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

It is common for companies in Hong Kong to enter into a private settlement with activists and the types of arrangement commonly agreed between the parties include:

- agreements to appoint shareholder activist's designees to the board of the directors;

- agreements to change the corporate governance of the company, such as modifying the size and composition of the board of directors of the company;
- agreements not to enter into certain transactions; and
- non-disparagement agreements.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

It is more common to have organised shareholder engagement efforts since the CG Code expressly recommends that listed companies shall have an ongoing dialogue with shareholders to communicate with them and encourage their participation. Also, the CG Code suggests that listed companies shall formulate a shareholders' communications policy. Many Hong Kong listed companies have carried out shareholder engagement as a matter of course and complied with the shareholder engagement efforts requirement stated in the CG Code. About 70 per cent of the Hong Kong companies also indicate that the board's shareholder communications strategies do not differ for different types of shareholders.

The outreach efforts typically entail:

- regular participation in investor conferences and roadshows (eg, MTR held more than 370 meetings with institutional investors and research analysts in Hong Kong and elsewhere during 2017)
- seminars and workshops for investors and industry associations;
- a specific hotline or email answering enquiries from individual shareholders; and
- regular dissimilation of the company's information to shareholders through email and websites.

23 Are directors commonly involved in shareholder engagement efforts?

Directors are expected to be commonly involved in shareholder engagement efforts in Hong Kong. According to section A.2.8 of the CG Code, the chairman should ensure that appropriate measures have been taken to provide effective communication with shareholders and their views are communicated to the board of directors as a whole. In the general meetings, the chairman of the board is expected to be present and answer shareholders' queries. As recommended in sections E.1 and E.1.4 of the CG Code, the board of the listed corporation shall bear the duty to maintain an ongoing dialogue with shareholders by, inter alia, communicating with shareholders in general meetings, and establishing a shareholders' communication policy.

Section O of the CG Code also provides that the company must disclose the procedures by which enquiries may be put to the board and sufficient contact details to enable these enquiries to be properly directed to the board in its Corporate Governance Report. The company shall also list out the procedures and sufficient contact details therein for shareholders putting forward proposals at shareholders' meetings. As such, directors are likely to be commonly involved in shareholder engagement efforts.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

With a view to promoting shareholders engagement, a listed company is required to disclose the following information in its Corporate Governance Report according to paragraph O of the CG Code:

- the way in which shareholders can convene an extraordinary general meeting;
- the procedure for sending enquiries to the board with sufficient contact details; and
- the procedure for making proposals at shareholders' meeting with sufficient contact details.

As such, shareholders may refer to the company's Corporate Governance Report and communicate directly with the board through the contact method indicated therein.

The board of director shall also establish a shareholders' communication policy and review it on a regular basis to ensure its effectiveness according to section E.1.4 of the CG Code. It is mandatory for the listed company to disclose whether these have been done in their interim reports and annual reports. If there is any deviation from the sections of the CG code, the reasons should be provided in the annual return.

Nevertheless, companies shall avoid selective disclosure. While it is understandable that where an activist has entered into dialogue with the board of the company and certain information shall be disclosed by the company to the activist, such information may fall under the scope of 'inside information' under section 307A(1) of the SFO, especially if other shareholders are not provided with such information. As such, any further dealing by the activist in the company's shares may amount to an act of insider dealing pursuant to sections 270(1)(e) and 291(5) of the SFO. In this regard, companies shall endeavour to avoid selective disclosure.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

Unless the shareholder disagrees, documents and information shall be sent by the company to its shareholders in electronic form according to section 831 of the Companies Ordinance and Rule 2.07A of the Listing Rules. Further, according to sections 833 and 573 of the Companies Ordinance, the company may communicate with its shareholder and publish the notice of general meeting on its website if the srticles expressly permit it to do so and the shareholders agree to it.

According to Rule 13.39(4) of the Listing Rules and section E.1.2 of the CG Code, companies must solicit votes from shareholders at a general meeting by poll unless the chairman decides to allow a resolution relating to a purely procedural or administrative matter to be voted by a show of hands. The listed company must also announce the meeting's poll results as soon as possible but in any event at least 30 minutes before the earlier of either the commencement of the Exchange's morning trading session or any pre-opening session on the business day after the general meeting.

Regarding the method to solicit support from other shareholders, an open letter is a common tool in Hong Kong. Nevertheless, there is an inherent risk in publishing an open letter. If the open letter contains any

false or misleading information about securities or futures that is likely to induce investment decisions or have an impact on the price and the activists knowingly, recklessly or negligently disseminate the false and misleading information, activists may be held criminally liable under sections 277 and 298 of the SFO and shall be liable to pay compensation to those who have suffered as a result of the wrongful information.

For instance, Andrew Left of Citron Research was found criminally liable by the Court of Appeal under section 277 for his false allegation in his research report that Evergrande Real Estate Group Limited was insolvent and had consistently presented fraudulent information to the public. The share price of Evergrande fell sharply on the same day following the publication of the report. As such, Andrew Left was banned from trading for five years and ordered to disgorge his profit of HK$1,596,240 from shorting shares of Evergrande and to pay the SFC investigation and legal costs.

It is noteworthy that the Court of Appeal specifically indicates that, when considering whether an unlicensed individual, namely Andrew Left, negligently disseminated the false and misleading information, the standard of care should be one that is comparable to a market commentator or analyst. Section 277 of the SFO creates a duty of care on any and all persons who choose to disseminate information that is likely to impact on the market with a view to maintaining the integrity of the market and protecting the investing public. In view of the above, both individual activists and institutional activists shall carry out reasonable steps to ensure that the information in relation to their investee company is true and not misleading before the publication of such information.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

According to section 366 of the SFO, all listed companies shall keep and allow shareholder's inspection of the register of interests in shares (including both registered interest or beneficial interest) and record any change therein with a view to enabling members of the public to ascertain the identity and the particulars of persons who are the true owners of voting shares in the listed corporation.

Under section 340 of the SFO, any shareholder and the investing public may inspect the register for free and upon payment of HK$10 respectively. Shareholder and the investing public may also require a copy of any registrar upon payment. In the case of the inspection request being rejected, the Court of First Instance may order and compel an immediate inspection of it.

It should be reminded that, under section 329 of the SFO, listed corporations are empowered to investigate the beneficial ownership of interests in its voting shares and the persons subject to investigation are obliged to give particulars of the beneficial ownership of interests. Upon receiving the particulars as to the beneficial ownership, the listed corporation shall notify the Exchange of the same in accordance with section 330 of the SFO.

If listed corporations do not proactively investigate the beneficial ownership of its shares, shareholders may request the company to do so under section 331 of the SFO and failing which the listed company will commit an offence and will be liable to a fine.

ONC Lawyers 柯伍陳律師事務所

Sherman Yan
sherman.yan@onc.hk

Dominic Wai
dominic.wai@onc.hk

19th Floor, Three Exchange Square
8 Connaught Place, Central
Hong Kong
Tel: +852 2810 1212
Fax: +852 2804 6311
www.onc.hk

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

In Hong Kong, the current hot topics in shareholder activism are the two recent high-profile shareholder activist campaigns instituted by Elliott and PAG.

The primary aim of Elliott's campaign is to oppose a placement agreement proposed by Bank of East Asia. Elliott filed an unfair prejudice petition against the Bank of East Asia on 18 July 2016 (Elliott International LP v Bank of East Asia Ltd (No 2) (HCMP 1812/2016) and successfully sought an order for discovery of documents in relation to the private placement on 28 August 2018. The trial of the unfair prejudice petition has been fixed for 40 days starting on 4 May 2020.

Another high-profile campaign is raised by a private equity firm PAG against Spring REIT. In late 2017, PAG wrote to the SFC and the Exchange and urged them to take appropriate actions against Spring REIT since Spring REIT intended to acquire 84 UK roadside properties that were leased to a car servicing chain Kwik Fit while its original portfolio mainly consisted of premium office assets in Beijing.

In September 2018, PAG offered to buy out Spring REIT for HK$5.24 billion and intended to appoint a new manager thereafter because of the material underperformance of Spring REIT, namely underperforming the Hang Seng REIT Index by 41.6 per cent since its IPO. Nevertheless, this attempt failed. It remains to be seen whether PAG will resort to taking legal actions against Spring REIT.

Ireland

Ciaran Healy and Naomi Barker
Matheson

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The Companies Act 2014 (the Companies Act) applies to all Irish incorporated companies and became effective on 1 June 2015. The Office of Director of Corporate Enforcement was established under the Company Law Enforcement Act 2001 to enforce and encourage compliance with company law. The Companies Registration Office is the body responsible for, among other things, the incorporation of companies, registration of business names, filing obligations and ensuring certain information is publicly available.

The Irish Takeover Rules are made by the Irish Takeover Panel under the powers granted to it by the Takeover Panel 1997 Act and by the European Communities (Takeover Bids (Directive 2004/25/EC)) Regulations 2006, as amended. They apply to public companies incorporated in Ireland whose shares are, or have in the previous five years been, traded on Euronext Dublin (formerly known as the Irish Stock Exchange), the London Stock Exchange, the New York Stock Exchange or the NASDAQ. The Irish Takeover Panel is responsible for ensuring compliance with the Irish Takeover Rules.

Companies with primary listings on Euronext Dublin (formerly known as the Main Securities Market of the ISE) are subject to continuing obligations under the Euronext Dublin – Rule Book II : Listing Rules, which regulate matters such as: (i) disclosure of information, (ii) shareholder approval of significant transactions, (iii) shareholder approval of related-party transactions, and (iv) terms and conduct of capital raisings.

Companies with a primary listing on Euronext Dublin are also subject to the continuing obligations set out in the Transparency (Directive 2004/109/ EC) Regulations 2007 (as amended) (Transparency Regulations) concerning the disclosure of financial information and significant shareholders. The Central Bank of Ireland is the administrative authority for the purpose of these regulations.

These companies must also comply with the UK Corporate Governance Code issued by the Financial Reporting Council (the Code) and the Irish Corporate Governance Annex (the Irish CG Annex), or explain in their annual reports why they have not done so.

Companies with a secondary listing on Euronext Dublin are subject to very few continuing obligations. These are largely related to disclosure of capital changes and maintaining free float requirements.

Regulation (EU) 596/2014 on market abuse (MAR) applies to companies listed on Euronext Dublin and Euronext Growth (formerly known as the Enterprise Securities Market). It principally regulates insider dealing, disclosure of inside information, dealings by directors and market conduct.

The Euronext Growth Rules apply to companies listed on Euronext Growth – the Irish equivalent of the AIM market. The continuing obligations under the Euronext Growth Rules are more limited than Euronext Dublin. For example, shareholder approval of transactions is not required unless they constitute a fundamental change of business.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Shareholder activism remains relatively underdeveloped in Ireland as compared with the United States. However, there are signs of change and there have been a growing number of domestic examples of activism in recent years. According to a report prepared by Lazard in the third quarter of 2018, although activity is highest in the United States, Europe has continued to be a focal point of activist attention. For example, Cevian Capital, Europe's biggest activist investor, built a stake in Irish listed company CRH plc, in early 2019. Cevian owns stakes in a range of blue-chip European companies.

The chance of success of an activist campaign depends largely on the key vulnerability factors of the relevant company such as: (i) companies experiencing significant change; (ii) board composition or remuneration issues; (iii) earnings underperformance; or (iv) undervalued companies. One key factor that has impacted companies in Ireland is Brexit. Now that Brexit is imminent, market uncertainty and volatility is set to continue, at least in the short to medium term. The volatility caused by Brexit presents a number of practical challenges for companies particularly certain smaller Irish-listed companies that are heavily reliant on the UK market. This could lead to further activist campaigns.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

At an Irish macro and public level, there is still a general market perception that shareholder activism is comprised predominantly of hostile and agitating corporate raiders whose primary goal is to cause disruption for short-term gain.

However, with the growing number of high-profile international and domestic examples of activism, it has increasingly become an issue for consideration by Irish executives and shareholders during the past few years and there is now a greater understanding that no public company in any particular sector is completely immune or insulated from activist campaigns.

At boardroom and analyst level, there has also been a growing awareness and acceptance of the potential benefits of activism as demands for increased returns continue. There appears to be a wider

recognition that activism can manifest itself in many different forms and involve many different categories of activists across any industry sector. There is also a growing appreciation of the constructive role that activists can play in effecting corporate change including most notably driving shareholder value.

However, one group that is worth flagging are the smaller Irish companies listed on Euronext Dublin. Given the relative smaller size of a number of companies listed on Euronext Growth, they are clearly more susceptible to activist influence and demands. There are also a group of Irish companies listed on NYSE and NASDAQ. Shareholder activism for those Irish companies tends to be aligned with activism activities and behaviour in the US rather than Ireland or the UK but such companies also need to be familiar with Irish company law and governance requirements.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

In recent years, the Irish market has seen a broad variety of activists ranging from individual shareholders to international investment firms or hedge funds and from proxy advisory firms to the Irish Government itself through their shareholdings in the Irish banks.

However, the majority of activist campaigns have originated from international investment firms or hedge funds. With the growing presence and influence of the proxy advisory firms, institutional investors are expected to be more vocal over the coming years, particularly in relation to 'say on pay' .

As regards the Irish companies listed on the NYSE or NASDAQ, activists tend to be based in the United States or in other international jurisdictions.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

Shareholder activism has focused primarily on board composition and remuneration including in particular calls to separate the roles of chairman and chief executive officers. Corporate governance issues, underperformance by management and inflated executive pay are generally perceived to be the main drivers for unseating board members. This was evident in the activist campaigns relating to Elan Corporation, Kingspan and Independent News & Media.

Irish companies are therefore scrutinising board composition and carrying out self-assessment checks more regularly.

Some other corporate changes that activists have sought in Ireland include demanding strategic change such as the sale or spin-off of a business division or financial change in the form of dividends or share buybacks. One notable high-profile example of an activist promoting corporate change was Orange Capital's attempt to persuade C&C Group to divest itself of its US interests. It is reported that Orange Capital initially approached C&C privately with a presentation on their proposals before the proposal entered the public domain.

Actavis acquired Irish company, Allergan, in 2015. This deal came about following a long-running hostile takeover campaign related to Allergan led by Valeant Pharmaceuticals and Bill Ackman.

The most high-profile example of socio-political activism relates to the Irish banks that were recapitalised by the Irish Government during the financial crisis. The boards of AIB, Bank of Ireland and Permanent TSB have all been the subject of some degree of public scrutiny and protest at their annual general meeting (AGM) of shareholders given the public interest in the banks. While socio-political activist campaigns are not yet widespread, Irish companies are increasingly aware of corporate social responsibility (CSR) issues and the majority of Irish public companies proactively provide information on their CSR policies and initiatives to shareholders.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

No matter what form of activism is used, the final goal is to effect change, whether at a management, operational or strategic level. Activism in Ireland often takes the form of private informal intervention in the pursuit of corporate change. Often the most successful activist campaigns in the Irish market are fought and won in a more subtle private engagement with the board. There is certainly a view among many activists that the most successful campaigns are the ones you never read about.

There is also a clear cost benefit to engaging in a round of meetings and telephone calls rather than a costly and protracted proxy solicitation campaign. Moreover, boardrooms are increasingly aware of the importance, both legally and optically, in listening to the views of shareholders. There is growing awareness that maintaining dialogue between activists and boardrooms is key and that often compromise is the best form of defence to a particular activist. Usually, it is only when the board reacts negatively to a request, or a series of requests, that the situation becomes more confrontational.

Clearly an effective tool for an activist is the use of the public domain as a forum for trying to initiate change. That can take the form of PR battles, open letters or press releases but more often consists of requisitioning general meetings, proposing resolutions and, in particular, directors changes, at the AGM or voting against resolutions.

In contrast to the United States, litigation is not generally regarded as a key tool for activist campaigns in the Irish market given the costly and relatively unpredictable nature of litigation proceedings. One exception to this was Petroceltic International's largest shareholder, Worldview Capital Management, initiating legal proceedings against it before it went into examinership.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

The Companies Act reserves various decisions for the approval of shareholders. An ordinary resolution is passed by a simple majority of the shareholders and a special resolution is passed by at least 75 per cent of the shareholders. As is the case in the United Kingdom, these thresholds are determined by reference to those shareholders who vote at the meeting so often can be passed by a far smaller percentage of the aggregate shareholder base.

Ordinary resolutions are usually required to carry out routine, less contentious, business. This includes matters such as authorising directors to allot shares and ratifying board decisions. In contrast, special resolutions are required for more significant matters such as altering a company's constitution, disapplying pre-emption rights, varying share capital or reducing share capital.

If a shareholder wants to make a proposal, it can requisition an extraordinary general meeting (EGM) if at least 5 per cent of the shareholders with voting rights approve such proposal. Where shareholders hold 3 per cent or more of the total voting rights, there is now also a statutory right to put forward items on the agenda for consideration and approval at general meetings. There are, however, a number of important conditions that must be satisfied in order to permit shareholders to exercise these rights. These include: (i) a justification for the inclusion of

the item or a draft resolution to be adopted at the general meeting; and (ii) circulation in sufficient time to ensure the relevant matter is received by the company at least 42 days before the meeting to which it relates.

Under Irish law, shareholders of a listed company currently have no 'say on pay' right to vote on the directors' remuneration report or remuneration policy unless such right is provided for in the particular company's constitution. However, once the Shareholders' Rights Directive (the Directive) (which came into force on 9 June 2017) is transposed into Irish law, shareholders will be able to vote on director remuneration where the company is listed on an EU-regulated market. First, they will be entitled to vote on the remuneration policy and, second, they will be entitled to vote on the remuneration report. The vote on the remuneration policy is likely to be binding. The vote on the remuneration report will be advisory. The Directive must be transposed into Irish law by 10 June 2019.

The vast majority of Irish companies on Euronext Dublin proposed resolutions to approve a remuneration report in 2018. Each of those companies classified the resolution as a non-binding advisory resolution only.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Shareholders may nominate directors for election to the board by requisitioning the directors of that company to convene an EGM for that purpose or by tabling a resolution for consideration at the AGM. The procedure for doing this is set out in questions 7 and 9.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

All general meetings, other than the AGM, are deemed to be an EGM. Notice must be given of each general meeting to every shareholder, director and the secretary of the company. The different categories of resolutions are referred to in question 7.

In respect of listed companies, shareholders holding 5 per cent or more of the company's share capital have the power to compel the directors to convene an EGM. The requisition must state the business to be transacted at the meeting. Where an EGM has been validly requisitioned, the directors must convene that EGM within 21 days to be held within two months of the requisition. Where the board of directors fail to convene the EGM within 21 days, the persons who have requisitioned the EGM may convene the meeting themselves.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Under Irish law, duties that relate to the conduct of a company's affairs, such as director duties, are generally owed to the company itself rather than to individual shareholders. Shareholders are therefore not generally permitted to bring an action on behalf of the company as the proper plaintiff in an action in respect of an alleged wrong done to a company is the company (ie, the Irish Courts apply the rule in *Foss v Harbottle*).

There are a limited number of exceptions to that principle and where such exceptions can be relied upon, shareholders may be permitted to institute a derivative action. It is important to remember that, much like the UK, a derivative action is not an action by a shareholder in its own capacity but rather on behalf of all the other shareholders.

The ability to bring a derivative action is dependent on the company itself having a claim and obtaining the leave of the Irish courts to commence the derivative action. In making a determination, the court is likely to consider whether the action should be brought by the shareholder personally and to seek the views of the other shareholders. These requirements effectively serve as defence measures to reduce the likelihood and frequency of derivative actions.

The wrongdoing will usually have to relate to: (i) an act that is illegal or ultra vires; (ii) an irregularity in the passing of a resolution; (iii) an act purporting to abridge or abolish the individual shareholder's rights; or (iv) an act that constitutes fraud against the majority and the wrongdoers are in control of the company.

There is also an onus on the plaintiff shareholder to demonstrate they have a realistic prospect of success in establishing the company was entitled to the remedy and that they fell within one of the four exceptions noted above.

There is no framework in Ireland to formally facilitate class actions. The closest procedures under Irish law to class actions or multi-party law suits are 'representative actions' or 'test cases'. A representative action is where one claimant or defendant, with the same (as opposed to similar) interest as a group of claimants or defendants in a particular action, institutes or defends proceedings on behalf of that group. Any relevant judgment or order will usually bind all claimants or defendants represented.

The more common option in Ireland for multi-party litigation is usually a test case. A test case can arise where numerous separate claims arise out of the same circumstances. For example, in 2008, the Irish Commercial Court was faced with more than 65 separate claims related to the fraudulent investment operations run by Bernie Madoff. The Irish Commercial Court decided to take forward two cases from individual shareholders and two by fund shareholders and stayed the remaining cases pending resolution of the four test cases.

There is no such action as a strike suit under Irish law but minority shareholders are afforded protection under section 212 of the Companies Act. Under this provision, a shareholder may apply to the court by petition for relief where the affairs of the company are being conducted, or the powers of the directors are being exercised, in a manner that is oppressive to the shareholder or in disregard of the shareholder's interests. If the court is of the opinion that the shareholder's action is well founded, it may make such orders as it sees fit, including: (i) directing or prohibiting any act or cancelling or varying any transaction; (ii) the purchase of the shares of any shareholders by other shareholders or by the company itself; or (iii) compensation. The court may also grant interlocutory relief. The nature of conduct required for conduct to be held oppressive or in disregard of the shareholder's interests will be judged by objective standards and there is no requirement to prove bad faith. It is also possible under section 569(f) of the Companies Act for a shareholder to apply to the court for the winding up of the company for the same reasons as above, that is, where the affairs of the company are being conducted, or the powers of the directors are being exercised, in a manner that is oppressive to the shareholder or in disregard of the shareholder's interests.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

In contrast with directors, whose duties are referenced in question 17, shareholder activists do not owe any fiduciary duties to the company.

Compensation

12 | May directors accept compensation from shareholders who appoint them?

A director may be separately remunerated by a shareholder who nominates or designates them but it would be unusual for an Irish-listed company. In a situation where directors are also employed by a shareholder, they need to be particularly mindful of their director's duties and the need to avoid any conflicts of interest.

Directors of Irish-listed companies are remunerated for their services by the company. Best practice for listed companies under the Code is to establish a remuneration committee to determine directors' remuneration. The Code recommends that a non-executive director's remuneration package should not include the granting of share options. In exceptional cases where the remuneration package does include options, advance shareholder approval must be obtained and where these options are exercised, the non-executive director must hold the shares for at least one year after leaving the board.

Mandatory bids

13 | Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

Under the Irish Takeover Rules, a shareholder is required to make a mandatory offer (under Rule 9) in the following circumstances: (i) the shareholder, or any persons deemed to be acting in concert with it, acquires 30 per cent or more of the voting rights in the company, or (ii) the shareholder's holding, or any persons deemed to be acting in concert with it, is 30 per cent or more of the voting rights in the company, but less than 50 per cent of the voting rights, and increases by more than 0.05 per cent of the aggregate percentage voting rights in that company in any 12-month period.

Any shareholder that cooperates with other shareholders needs to consider the implications of acting in concert for mandatory bid and other Irish Takeover Rules purposes.

The Irish Takeover Rules do state that the action of shareholders voting together on particular resolutions may not of itself lead to a mandatory offer obligation but the Irish Takeover Panel may, in certain circumstances, hold that such joint action indicates that there is a group acting in concert with the result that purchases by any member of the group could give rise to such an obligation. The Irish Takeover Rules do not, however, elaborate, in the same manner as the UK Takeover Code, on whether shareholders who propose a 'board control-seeking' resolution will be presumed to be acting in concert.

'Acting in concert' is defined under the Irish Takeover Rules and includes a specified list of persons that are presumed to be acting in concert with a party to a bid or takeover unless the contrary is established to the satisfaction of the Irish Takeover Panel. In practice, the Irish Takeover Panel will always look at the facts of a particular situation in order to establish what actions should be treated as those of the bidder or target (as the case may be).

Two or more persons will be deemed to be 'acting in concert' as respects a takeover or other relevant transaction, including a substantial acquisition of securities if they co-operate on the basis of an agreement, either express or tacit, either oral or written, aimed at:

- either:
  - the acquisition by any one or more of them of securities in the relevant company concerned; or
  - the doing, or the procuring of the doing, of any act that will or may result in an increase in the proportion of securities in the relevant company concerned held by any one or more of them; or
- either:
  - acquiring control of the relevant company concerned; or
  - frustrating the successful outcome of an offer made for the purpose of the acquisition of control of the relevant company concerned.

The Irish Takeover Rules contain a non-exhaustive list of persons who are deemed to be acting in concert (such as affiliates, directors, etc) for the purposes of both the Irish Takeover Rules and the Substantial Acquisition Rules (SARs). However, beyond that, the question is one of fact to be considered by reference to the relevant facts of each particular case.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Shareholders with interests in Irish public companies listed on an EU-regulated market such as Euronext Dublin and the main market of the LSE are required to comply with the Transparency Regulations. Under the Transparency Regulations, a person is obliged to notify a listed company where the percentage of voting rights that it holds reaches, exceeds or falls below 3 per cent and each 1 per cent threshold thereafter. The notification to the company must be made as soon as possible, and within two trading days for an Irish company.

Shareholders with interests in Irish public companies, not listed on an EU-regulated market, such as Euronext Dublin, AIM, NYSE and NASDAQ, must comply with the disclosure requirements under the Companies Act. The statutory disclosure regime requires notification of interests in, and changes to interests in, 3 per cent or more of the 'relevant share capital' or of any class of 'relevant share capital'. The obligation arises where a person knowingly acquires an interest, or knowingly ceases to be interested, in shares or becomes aware that he or she has acquired an interest, or ceased to be interested, in shares. The notification must be made in writing to the company, in a prescribed form, within five days.

The disclosure obligations under the Irish Takeover Rules apply when a listed public limited company is in an offer period. During an offer period, any person who is interested in 1 per cent or more of any class of voting securities is required to disclose all further dealings in securities of that class. As with the SARs, a person's holding is aggregated with the holdings of persons with whom it is 'acting in concert'.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

Where a party is seeking to avoid triggering the Companies Act disclosure requirements, this can potentially be achieved through the use of contracts for differences (CFDs). Entry into a derivative referenced to the shares of a company is not counted for the purposes of the Companies Act disclosure requirement unless it is coupled with the acquisition of an interest in the relevant shares to which the derivative is referenced or the party entering into the derivative acquires the ability to exercise rights in relation to those shares. Accordingly, if a party enters into a CFD without acquiring such rights, it can avoid coming under an obligation to disclose and it may therefore be possible for an activist shareholder to build a substantial stake in a company without triggering a disclosure requirement under the Companies Act.

For the purposes of determining whether or not a party has triggered the 1 per cent threshold under the Irish Takeover Rules (as referenced in question 14), derivatives giving the party a long position in the relevant shares are counted. Once the 1 per cent threshold is

reached then all dealings in derivatives (long and short) must also be disclosed in the same way as dealings in the relevant shares.

Insider trading

16 | Do insider trading rules apply to activist activity?

As set out in question 1, the MAR applies to companies listed on Euronext Dublin and Euronext Growth. TheMAR prohibits activities such as insider dealing and market manipulation, while also imposing obligations on issuers of securities or financial instruments regarding the disclosure of inside information and the maintenance of insider lists.

In terms of dealings on non-regulated markets, the provisions in Chapters 1, 2 and 4 of Part 23 of the Companies Act apply to public companies, which effectively makes public companies subject to requirements concerning prospectus, market abuse and transparency rules, most of which are derived from European legislation.

It is clear that trading on the basis of knowing inside information could constitute insider dealing.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

Directors are not required to consider an activist proposal in a different manner to other board decisions.

The Companies Act sets out the fiduciary duties that directors owe to the company. These duties include a duty to act in good faith and in the interest of the company, to act honestly and responsibly, and to avoid conflicts of interest. These duties are owed to the company and the company alone. Directors appointed by shareholders may in the performance of their duties have regard to the interests of the shareholder but this will be subject always to the overriding fiduciary duties owed to the company.

While directors may be very unwilling to deal with an activist shareholder, they will ultimately need to decouple their personal opinions and ask themselves: is the proposed action in the best interests of the shareholders?

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

It is more important than ever for Irish boards to be ready to deal with shareholder activism. While activism along with issues such as Brexit, cybersecurity, regulatory challenges and reputation risk are occupying the minds of Irish boardrooms, the time invested by boards in considering and preparing for it varies widely.

Responding effectively to activist shareholders requires advance preparation and active investor engagement on issues of importance to investors. It is no longer sustainable for companies to 'just say no' to an activist campaign. While some activist attention can be unwanted, companies and their boards should not respond dismissively to activist proposals.

Companies should focus carefully on regular shareholder communications and be prepared to respond to activist campaigns by assessing, on at least an annual basis, how susceptible the company is to an activist campaign, by whom and in what particular areas. Companies need to focus on communicating a consistent and clear corporate strategy and proactively deal with earnings shortfalls or other adverse developments. Shareholder engagement on an ongoing basis can help lay the vital groundwork for better investor relations to ensure a company has support from a wide cohort of the shareholder base.

Other advice includes monitoring the share register, adhering to corporate governance best practice, maintaining a unified board consensus and being prepared for all eventualities at the AGM.

Defences

19 | What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Structural and other defences are not common in Ireland. A target board must ensure at all times they observe their fiduciary duties to act in the best interests of the company. The Irish Takeover Rules dictate that directors of a relevant target must act only in their capacity as directors and not have regard to their personal interests. At any time during the course of an offer, or when the board has reason to believe that an offer may be imminent, the Irish Takeover Rules (General Principle 3 and Rule 21) prohibit companies from taking any action that would or might frustrate an offer or deprive shareholders from the opportunity of considering an offer. Unless the consent of the Irish Takeover Panel is obtained (and, in some circumstances, shareholder approval), putting in place structural defences such as poison pills during the offer period is not permitted under the Irish Takeover Rules as they could be deemed to constitute frustrating actions. Frustrating actions include issuing new shares or options, disposing or acquiring material assets, or entering into non-ordinary course contractual arrangements.

A number of Irish holding companies with listings in the United States have, however, adopted automatic shareholder rights plans that, in general terms, work by imposing a significant penalty upon any person or group that acquires 10 per cent or more of the outstanding ordinary shares of the company without the prior approval of the board of directors.

Staggered boards are not a feature of Irish companies. Directors of Irish companies can be removed by an ordinary resolution under section 146(1) of the Companies Act. As noted above, the Code also applies to companies listed on Euronext Dublin and provides that directors of relevant companies should be elected or re-elected annually.

Proxy votes

20 | Do companies receive daily or periodic reports of proxy votes during the voting period?

The registrars of Irish companies have the ability to provide daily proxy update reports to the company ahead of any general meeting. As a large number of proxy votes tend to be made in the week leading up to the general meeting, daily updates reports are more common during this period.

Prior to proxy votes being cast, companies may engage with shareholders and, in particular, institutional shareholders or investor protection committees, to seek them to vote in favour of resolutions.

Proxy votes are typically granted in favour of the company chairman and are confidential in the lead up to the general meeting.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

It is very common for companies to engage with activist investors privately in the first instance as a means of avoiding public and more costly action at the outset. This remains the preferred course of action in Irish shareholder activist scenarios. If an activist succeeds with its regulations, it typically results in either an announcement from the company that it is considering a particular course of action such as a strategic review or a shareholder proposal being tabled at the next AGM.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

Organised shareholder engagement has increased during the past few years but does tend to vary quite considerably from company to company.

As referenced in question 23, ongoing dialogue with shareholders is a core principle of the Code. The UK Stewardship Code also promotes effective engagement from institutional shareholders in dealing with companies.

As noted at question 6, activists ordinarily prefer to engage on a more private, informal and amicable basis. While companies are increasingly willing to engage with shareholders, they are not usually minded to cede to requests for board seats and other corporate changes, at least in the short term.

23 Are directors commonly involved in shareholder engagement efforts?

Ongoing dialogue by the board with shareholders is a core component of the Code. The main principle of this is that shareholder dialogue should be based on the mutual understanding of objectives. The Code sets out that 'the board should keep in touch with shareholder opinion in whatever ways are most practical and efficient'.

Very often most shareholder engagement takes place via the chairman, CEO or CFO. In order to ensure the board is sufficiently engaged, the board must state in the annual report the steps taken to ensure that the directors, especially the non-executive directors, have engaged with shareholders. The Code, in particular, promotes engagement by the chairman and non-executive directors with shareholders. For example, the chairman is expected to discuss governance and strategy issues with major shareholders.

As noted at question 3, the Code encourages active board engagement with shareholders and the UK Stewardship Code promotes active engagement by institutional shareholders with the board.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

As in the United Kingdom, an Irish-listed company must not ordinarily selectively disclose information to shareholders. Under the MAR, an Irish-listed company is expected to disclose 'inside information' to the market as soon as possible. Inside information includes specific or precise unpublished information relating to a particular issuer or particular securities that, if made public, would have a significant effect on the price of any securities.

The MAR recognises that that inside information can be legitimately disclosed to a shareholder or a potential shareholder for market sounding purposes in order to measure interest in a potential transaction, its size or pricing. However, there are onerous requirements including the need to obtain the shareholder's consent and the need for the company to keep detailed records of the market soundings.

The MAR provides that companies may legitimately delay disclosure of inside information to the public provided all of the following conditions are met: (i) immediate disclosure is likely to prejudice the company's legitimate interests; (ii) delay of disclosure is not likely to mislead the public; and (iii) the issuer is able to ensure the confidentiality of the information. Selective disclosure is also permitted to a shareholder if the shareholder owes the company a duty of confidentiality and requires the information to perform their functions.

There is in any event an obligation on companies to maintain insider lists for deal-specific or event-specific matters.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

Selective communications by a company to a discreet number of shareholders often fall within the meaning of 'inside information'. Shareholders are prohibited from dealing on the basis of such information under the MAR. Larger institutional shareholders usually have appropriate wall-crossing procedures in place to ensure that inside information can be received by a small number of relevant people within the organisation without restricting the dealing teams. Companies also need to be aware that where there is media speculation or market rumour regarding a company, they are required to assess whether a disclosure or announcement obligation arises.

Companies are increasingly turning to proxy solicitation and investor relations specialists to provide shareholder analysis reports, monitor trading movements and competitor analysis.

There are systems a company can put in place to facilitate communication with its shareholders. Information booths can be set up at AGMs dealing with questions from individual shareholders. However, the type of information to be shared at the booths should be considered carefully in advance. Similarly, a company may set up a Q&A section on its website where frequently asked questions are answered prior to an AGM.

The use of social media platforms by activists in Ireland is still not common.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

Every company is required to keep up-to-date statutory registers with details of the legal owners of the shares in the company. The shareholders have a statutory right to inspect and receive copies of the statutory registers kept by the company. As regards other persons,

such as creditors, employees or members of the public, the register of members is open to inspection on the payment of a fee.

Although companies do not have to recognise the beneficial holders of shares, under section 66 of the Companies Act, there is nothing precluding a company from requiring a member or a transferee of shares to furnish the company with information as to the beneficial ownership of any share when such information is reasonably required by the company. The beneficial interest may also be required to be disclosed on foot of a court order.

Even though beneficial interests are not being recorded in the register of members, a company may not ignore beneficial interests of which it has actual notice. These interests must be disclosed and recorded in a register, known as a 'register of interests'. Under section 261 of the Companies Act, directors and secretaries must notify the company in writing of their interests in shares or debentures of the company. When a company receives information from a director or secretary, it must enter that information in the register of interests within three days.

To the extent that a plc receives information relating to its shares on the back of issuing a disclosure notice under the Companies Act, it is also required to maintain a list of such beneficial shareholders in its statutory registers.

Separately, the European Union (Anti-Money Laundering: Beneficial Ownership of Corporate Entities) Regulations 2016 came into effect on 15 November 2016, meaning that Irish companies, except companies listed on Euronext Dublin and Euronext Growth, must gather and maintain information on individuals described as their ultimate beneficial owner.

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

One relatively new development has been the increased activist activity on the part of proxy advisory firms.

Institutional Shareholder Services (ISS) advises large investors on corporate governance issues. Recently, ISS recommended that the shareholders in Malin vote against the company's remuneration arrangements. Woodford Investment Management, which holds a 23 per cent stake in the company, and ISIF voted by proxy against the proposed pay and severance plans. This led to a board and management overhaul and forced the company to put a strategy in place identifying four 'core assets' in its portfolio of investments.

Another recent high-profile campaign was the acquisition by Cevian, Europe's largest activist investor, of a stake of just less than 3 per cent in Ireland's largest multinational, CRH. It is understood that Cevian sees CRH as being undervalued by the stock market, with margins trailing in comparison to competitors, having little organic revenue growth and a strategy based on making acquisitions. Some predictions speculate that Cevian will continue to build its stake in the company with the aim of taking a seat on the board and looking for some asset sales and cost efficiencies in order to improve margins. Other predictions have been that given most of CRH's earnings are coming from the United States. Cevian may press them to look at a partial listing of its North American unit in New York to unlock value. Cevian is expected to engage with management after CRH's annual results this year.

Brexit is also a key concern currently impacting market volatility that could create new opportunities for activists who can benefit from the unpredictability. Steven Balet, head of corporate governance and activist engagement at FTI Consulting's strategic communications arm, has said some activist firms were currently eyeing Ireland, which has a 'permissive' regulatory environment that could favour their strategies.

Matheson

Ciaran Healy
ciaran.healy@matheson.com

Naomi Barker
naomi.barker@matheson.com

70 Sir John Rogerson's Quay
Dublin 2
Ireland
Tel: +353 1 232 2000
Fax: +353 1 232 3333
www.matheson.com

Israel

Amir Shachar
Shibolet with Raved, Magriso, Benkel & Co

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The primary sources of laws and regulations relating to shareholder activism and engagement are the Companies Law, 1999 (the Companies Law) (see question 7 for certain rights granted to shareholders under the Companies Law); the Companies Regulations (Written Voting and Position Statements), 1999; the Companies Regulations (Notification and Announcement of Public Company General Meeting and Special Meeting and Addition of Items to Agenda), 2000; the Securities Law, 1969 (the Securities Law); Securities Regulations (Periodic and Immediate Reports), 1970 and Securities Regulations (Transaction with a Controlling Shareholder), 2001.

The Companies Law applies to companies incorporated in Israel; companies incorporated outside Israel that have issued shares or bonds to the public in Israel will be subject to certain provisions of the Companies Law. The Companies Law, the Securities Law and the regulations of these laws have been legislated by the Israeli parliament (the Knesset), and are enforced mainly by the Israeli Securities Authority.

Additional sources of regulations that apply to institutional investors include: the Joint Investments in Trust Law, 1994; the Ordinance Supervision of Financial Services (Provident Fund) (Participation of Managing Company at a General Meeting), 2009 and the Circular for Financial Institutions of the Capital Market, Insurance and Savings promulgated by the Israeli Ministry of Finance. These sources determine, inter-alia, the mandatory duty of institutional investors to participate in shareholders meetings.

In addition, there are recommended rules of corporate governance and voting policies that have been drawn up by advisory bodies to institutional investors (such as Entropy Financial Research Services and Emda Financial Research) and also similar policies drawn by institutional investors. These rules and policies include reference to shareholder activism and engagement. The recommendations made by advisory bodies to institutional investors (especially Entropy) have a material influence on the outcome of the votes taken at general meetings.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Over recent years, including last year, there has been a surge in the involvement of shareholders in the operation and management of Israeli public companies traded on the Tel Aviv Stock Exchange. Nowadays, the shareholders, including the institutional investors, have evolved and are more sophisticated and professional. Also, we now see a phenomenon of institutional investors having set up special and designated departments dealing with institutional involvement.

It is important to state that this involvement is not limited to extreme situations, such as a crisis or insolvency or default in payment or suspicious transactions, but also with reputable companies capable of generating a higher added value for investors.

The institutional market realises its ability to influence matters affecting the quality of investment management, and institutional investors are becoming more and more involved, including by joining other activist campaigns, such as hedge funds.

In addition, a sharp and exponential rise has been occurring in the volume of money infused to hedge funds and institutional investors, enabling them to acquire larger stakes and carry out significant activist moves in the target companies.

Some of the hedge funds prepare detailed presentations analysing target companies, including recommendations on possible actions that will assist in increasing the companies' value. Such hedge funds engage with material shareholders in order to gain their support for activist campaigns.

Moreover, there is a drop in the number of companies that have a controlling shareholder (mainly dual companies in the hi-tech and life sciences sector). This makes it easier to carry out an activist campaign. At the end of 2010, 96 per cent of the non-dual companies were controlled by controlling shareholders or groups of control, and only one of the companies included in the Tel Aviv 100 Index was under distributed ownership. The average control interest in 2010 was 65 per cent; today some 90 per cent of the non-dual companies are under control of a controlling shareholder holding on average 51 per cent of the equity. The Tel Aviv 125 Index now includes 10 companies under distributed ownership; if we add dual companies, the present situation is that about 81 per cent of the companies are under control of controlling shareholders holding an average of 51 per cent of the equity on average.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

The Companies Law is considered a paradise for activist shareholders. Herein are some examples of the rights of shareholders under Israeli law, which allow them to influence the operation of a company:

- Minority shareholders have the right to veto key corporate decisions, including the appointment of external directors and approval of controlling shareholders transactions.
- Shareholders are given the option of demanding to assemble a general meeting in certain cases, adding issues to the agenda of a general meeting, including the appointment and dismissal of directors and presenting their position on matters on the agenda of a general meeting.

- The shareholders also have the right to provide the company with a position statement, which must be published by the company to the public on the distribution website of the Israeli Securities Authority and the Tel Aviv Stock Exchange.
- The shareholders are given the right to vote via an electronic voting system affording them easier access to shareholders meetings and increase their involvement.
- The legal environment provides minority shareholders with the opportunity to take steps against a controlling shareholder and/or the company's directors and officers, for example, by filing class actions or derivative actions.

Anat Guetta, chairperson of the Israeli Securities Authority, recently expressed her views at a conference held on 27 November 2018, stating that there is an increased trend of involvement on the part of Israeli institutional investors in becoming more active in the companies in which they invest, especially those without control interest. Guetta stated that this is an important and welcome trend. She said: 'I feel that the fact that institutional investors are finally assuming responsibility and becoming significantly more involved with their substantial holdings is a good sign for the market, which is what should be aimed for and how the capital market should appear in this process of structural change.'

Increased shareholder activism may be observed in dual companies and technological or life science companies, especially those lacking a control interest and having high cash balances or with a performance lower than comparable companies.

In view of the fact that this is a relatively new phenomenon, shareholders still have a somewhat suspicious attitude towards aggressive activist activities on the part of hedge funds, which sometimes may be regarded as opportunistic and thought to only make short-term considerations that may prejudice the benefit of the company. This is despite the fact that there are cases where cooperation between hedge funds and institutional investors has been noted. Institutional activist activity is most often perceived as a legitimate strategy to influence a company's behaviour especially with respect to corporate governance issues.

Shareholders activism may be identified in a large number of industries and sectors and in companies of various sizes, including some of Israel's major public corporations.

A lower level of shareholder activism is seen in the banking sector. There are several reasons for this lower involvement, such as:

- It is difficult to hold means of control over banks in Israel since one should receive the Bank of Israel approval to hold such means of control and also there is a maximum holding limit with an upper limit to holdings.
- The banks are subject to stringent regulation and many regulators, such as the Israeli Securities Authority, the Supervisor of Banks, the Governor of the Bank of Israel and the Supervisor of the Capital Market, Insurance and Savings.
- Each bank also employs a compliance officer, who is a senior executive, responsible for the bank's compliance with the provisions of the law and regulatory requirements.
- Banks in Israel are also subject to additional regulatory restrictions on their ability to modify their articles of association, thus making it more difficult for activist movements in this sector than in other public companies.

In view of this, the corporate governance in banks is highly developed and the financial results of the large banks also seem quite satisfactory, thus there is little incentive for significant shareholder activism.

In addition, the Remuneration Law for Officers of Financial Corporations (special approval and the disallowance of expenses for tax purposes owing to exceptional remuneration), which was enacted in 2016, has significantly limited senior bank officials' salaries by determining that the highest compensation that may be paid to an executive of a financial corporation shall not exceed 35 times the lowest salary paid to any of the coorporation's employees, and that the portion of an executive's salary in excess of 2.5 million Israeli new shekel per annum will not count as an employer's recognised expense.

The above does not imply that banks in Israel are immune from activist campaigns, just that the process has yet to mature.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

Activist shareholders may be divided into a number of groups:

- Certain hedge funds of varying sizes operate in Israel, and their number remaining almost constant in recent years.
- In recent years, we have seen involvement of giant American hedge funds that have been involved in activist moves with public corporations whose shares are traded on the Tel Aviv Stock Exchange or abroad (eg, Elliott with Bezeq and Starboard with Mellanox).
- There is an increasing trend of significant involvement on the part of institutional investors in public companies, which in some cases have been cooperating with hedge funds.
- A non-negligible part of activist activity is carried out by private investors who in the past were passive investors in the company and after being disappointed by the company's performance, or for other reasons, changed their approach. As opposed to hedge funds, which are considered highly sophisticated 'classic' activist entities that come to the company with prepared plans and potential directors, these private investors do not have the same resources and abilities and there are those who perceive them to be 'pseudo-activists' and occasionally, even 'extortionists'.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

The most common topic addressed in the field of institutional activism in Israel is the composition of the board of directors.

Institutional investors intervene in changes in the composition and size of the board of directors, usually by proposing to appoint external directors. Recently, we have even seen intervention in the identity of the person to be appointed as chairman of the board, as well as an attempt to dismiss external directors within their statutory period of tenure (three years).

Entropy, an advisory body for institutional investors, has a voting policy supporting institutional investors' intervention in matters of corporate governance, including putting up their own candidates to be appointed as external directors and supporting their candidacy.

Other areas with significant intervention on the part of institutional investors are the compensation policy for executives, approval of the executives' compensation packages and controlling shareholders transactions.

In 2018, Entropy emphasised the model of 'compensation fairness' with respect to executive compensation agreements. This model is based on industry- and company-size parameters including share performance over time. Entropy encourages the formulation of performance-based compensation agreements in order to provide an effective incentive for business result improvements and value to the shareholders. Entropy is usually reluctant with compensation agreements that could lead management to take extreme risks that improve short-term results but may be detrimental to shareholders in the long run.

In addition, in complex M&A transactions (such as Frutarom and IFF, the merger of Equital and Joel-Jerusalem Oil Exploration and the merger of Castro and Hoodies), Entropy requested that the companies

appoint an independent expert on behalf of Entropy to analyse the transaction in order to establish a voting recommendation.

At the same time, there remain a number of areas of institutional operation in the capital market still characterised by low to non-existent shareholder activism. In this context, Israeli institutional investors rarely file class and derivative actions concerning events taking place in companies in which they hold shares. The chairperson of the Israeli Securities Authority has said in this respect: 'I would have expected a greater presence of institutional investors with a wider outlook and in a more significant fashion.'

The most common areas of hedge fund activism are with regard to strategy changes in corporation (focusing on core activities and divestiture of underperforming assets), M&A (for example, pressuring for the sale of the company) and also occasionally dividend payments.

Hedge funds are aware that institutional investors are focused on ensuring that boards become diverse, have the relevant skills and experience to the specific business of the company and proper balance of independent directors. Hedge funds know to focus in their activist moves on issues related to corporate governance and in particular to the board of directors, thereby attracting institutional investors in their campaigns.

The most common areas of hedge fund activism are with regard to strategy changes in corporations (focusing on core activities), M&A and also occasionally dividend payments.

The effectiveness of shareholder activist moves has become more mature and efficient given that:

- shareholders are more sophisticated nowadays, with a much higher level of professionalism and natural maturity in shareholders' activism;
- institutional investors have set up specialist departments dealing with institutional involvement;
- a large portion of corporate shares are held by institutional investors, which have substantially increased their holdings in recent years;
- advisory bodies to institutional investors are placing a strong emphasis on corporate governance aspects;
- legislative amendments in recent years, such as amendments 16 and 20 of the Israeli Companies Law, have placed material powers in the hands of shareholders; and
- the distributed market structure has started to establish itself while enabling the shareholders to pressure companies into making various changes.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

The activist's toolbox is diversified and has many ways to increase pressure on the company to comply with the activist demand.

For example, an activist may act to publish a position statement on general meeting agenda items, or to request the company to call a special meeting, usually in order to change the composition of the board of directors or to ask the company to add an additional item on the agenda of a general meeting.

Under the Companies Law, shareholders are entitled to review various company documents, including general meeting minutes. Such documents assist activists in their campaigns. For further information regarding shareholders rights to receive information, see question 26.

Some activists use the media, which has shown interest in shareholders' activism – for example, headlines regarding the replacement of office holders in a public company or a letter to the board containing severe statements on the operation of the company's management. These publications create interesting media publications of struggle and drama, which are like music to the ears of the press. Such publication obviously influences the company and its directors and officers.

Some activists may also approach the Israeli Securities Authority with a detailed complaint against the company or its office holders to increase pressure on the company.

Additionally, some activists engage directly with the board or the management following a thorough analysis of the company and the market in which it operates. In such cases, the activists present either a comprehensive document or presentation, which includes inter alia vulnerabilities of the company's strategy and the advantages of the strategy proposed by the activist. Such a document may sometimes be sent in advance to the company's major shareholders and might persuade them to support the activist's position.

The specific choice of strategy is dependent on the identity of the activist, his or her objectives, the identity of the leaders of the company, its corporate governance quality and the company's maturity to handle shareholder activism.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

One or more shareholders holding at least 5 per cent of the issued capital and at least 1 per cent of the voting rights in the company, or one or more shareholders holding at least 5 per cent of the voting rights in the company, is/are authorised to require the board to assemble a special meeting whose agenda will be determined by him or her/them. The board is obliged to schedule the meeting within 21 days of the demand being submitted to it. Insofar as the board fails to call the meeting, the shareholders are authorised to call the meeting by themselves and the company is required to reimburse them the reasonable expenses incurred in connection with this.

One or more shareholders holding at least 1 per cent of the voting rights at the general meeting is/are authorised to request the board to include an item in the agenda of a general meeting to be held in the future, provided that the board determines that the item is appropriate for discussion at the general meeting. Such a shareholder's request as stated should be conveyed to the company between three to seven days after the summon for the meeting has been sent, depending on the type of meeting. A shareholder's request to include in a general meeting agenda nomination of a candidate as a director should include various particulars of the candidate as well as a declaration of the candidate's competence to serve as director, in accordance with the provisions of the Companies Law.

Any shareholder is authorised to submit a position statement to the company up to 10 days before the meeting is held, expressing his or her opinion in connection with the meeting agenda items. The position statement must be drafted in a clear and simple language and contain up to 500 words on each agenda item. A shareholder submitting a position statement, acting in concert with others for the purpose of voting at the general meeting on all or one of the items on the agenda, shall indicate this in the position statement, specifying the cooperation understandings and the identity of the shareholders party to the collaboration. In the event that the shareholder or some other person collaborating with him or her has a personal interest in the outcome of the vote at the general meeting, the nature of this personal interest shall be indicated.

The company must publish this position statement on the Tel Aviv Stock Exchange and the Israeli Securities Authority distribution websites.

The party submitting the position statement will bear sole legal responsibility for its content.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Shareholders are authorised to recommend directors for election to the board of a company in the general meeting by submitting a request for scheduling a meeting or adding an item to the agenda, as specified in question 7.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Shareholders may call a special meeting following the process set out in question 7. There is no legal procedure in public companies, as opposed to private company, in reaching all resolutions in a written manner in lieu of holding a general meeting.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

There are three main types of common shareholders' litigation:

- A derivative action, which is filed on behalf of the company;
- A class action, which is filed on behalf of a certain class, such as a class of shareholders; and
- An appraisal claim, which is filed following a full tender offer that includes a compulsory acquisition.

A derivative action can be filed by a shareholder or a director or a debtor pursuant to the conditions detailed in the Companies Law, including initial application having been made to the company (except, among other situations, under particular circumstances where the board is affected by a personal interest) requesting the company to file such claim. Insofar as the company rejects to file such claim, then plaintiff is allowed to submit a derivative action application on behalf of the company. The court will tend to certify the derivative action application if it determines mainly that there is prima facie evidence that there are merits to such claim and that the claim is to the benefit of the company and that the plaintiff is not acting in bad faith.

A derivative action may be filed in respect of any matter or issue, including a claim for compensation or disgorgement against directors and officers, third parties, other shareholders who has harmed the company, including the controlling shareholders and so on.

The Companies Law allows the Israeli Securities Authority to fund a derivative action, if requested by the plaintiff. If the Israeli Securities Authority is satisfied that the derivative action has a public interest and that there is a reasonable chance that the court will certify it as a derivative action, it may bear the costs of the plaintiff.

Whoever is authorised to file a derivative action is entitled to request the court, prior to or following submission of the application for approval of the claim, to instruct the company to disclose documents relating to certain issues of the company where there is a suspicion of wrongdoing by others that resulted in a loss to the company. This legal procedure is for the purpose of examining the merits of a potential derivative action. The court is authorised to approve this motion for disclosure if it is convinced that the applicant has provided an initial prima facie evidence for this preliminary stage and that the applicant is acting bona fide with respect to the motion.

Another litigious course of action is a class action. An application for approval to file a class action may be submitted in accordance with the Class Action Law, 2006. The Class Action Law specifies in its endorsement on what cause of action and against whom a class action can be filed.

According to the endorsement, a class action can be filed by a party having 'an interest in certain security', that is, allegations relating to securities must be involved. There are four preconditions, which the court must examine in order to certify a claim as a class action:

- the claim gives rise to substantial questions of fact or law common to the entire class and they are reasonably likely to be settled in favour of the class;
- the class action is the most efficient and equitable way of resolving the dispute other than by means of a regular claim;
- the court is persuaded that all members of the class are adequately represented; and
- the court is persuaded that the affairs of the members of the class will be managed in good faith.

Courts will tend to certify a class action where a wrongdoing has been demonstrated prima facie.

The Securities Law allows the Israeli Securities Authority to fund a class action, if requested by the plaintiff. If the Israeli Securities Authority is satisfied that the class action has a public interest and that there is a reasonable chance that the court will certify it as a class action, it may bear the costs of the plaintiff.

A person wishing to acquire shares of a public Israeli company and who would as a result of such acquisition hold over 90 per cent of the target company's voting rights or the target company's issued and outstanding share capital (or of a class thereof) is required by the Companies Law to make a tender offer to all of the company's shareholders for the purchase of all of the issued and outstanding shares of the company (or the applicable class). If:

- the shareholders who do not accept the offer hold less than 5 per cent of the issued and outstanding share capital of the company (or the applicable class) and a majority of the offerees that do not have a personal interest in the acceptance of the tender offer accepted the tender offer; or
- the shareholders who did not accept the tender offer hold less than 2 per cent of the issued and outstanding share capital of the company (or of the applicable class), all of the shares that the acquirer offered to purchase will be transferred to the acquirer by operation of law.

A shareholder who had his or her shares so transferred may petition the court within six months from the date of acceptance of the full tender offer, regardless of whether such shareholder agreed to the offer, to determine whether the tender offer was for less than fair value and whether the fair value should be paid as determined by the court. A petition of this sort may also be filed as a class action. However, an offeror may provide in the offer that a shareholder who accepted the offer will not be entitled to appraisal rights as described in the preceding sentence, as long as the offeror and the company disclosed the information required by law in connection with the tender offer. If the full tender offer was not accepted in accordance with any of the above alternatives, the acquirer may not acquire shares of the company that will increase its holdings to more than 90 per cent of the company's issued and outstanding share capital (or of the applicable class) from shareholders who accepted the tender offer.

The Supreme Court ruled in the case of *Atzmon v Bank Hapoalim Ltd* that the value of the target company in an appraisal claim followed by a full tender offer will be determined in accordance with the discounted cash-flow method.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 | Do shareholder activists owe fiduciary duties to the company?

There is no legal provision or case law in Israel that discuss this question. We believe that activist shareholders have no fiduciary duties or duty of care towards the company, as opposed to directors.

Having said that, under Israeli law, a shareholder who votes at a general meeting on amendments to the articles of association, increase of the share capital, merger and the approval of controlling shareholders transactions, must act in good faith towards the company and the other shareholders, and refrain from taking unfair advantage of his or her power in the company.

Furthermore, a shareholder who is aware that his or her voting decision will have a decisive effect on the resolution of a certain decision, will have a duty to act in an equitable fashion towards the company. Such obligation of equitability was discussed in an Israeli precedential case law in the *Bezeq* ruling (*Vardenikov v Elovitz*) handed down by the Supreme Court, establishing that this duty is placed between fiduciary duty and the duty to act in good faith.

Compensation

12 | May directors accept compensation from shareholders who appoint them?

In principle, directors may accept compensation from shareholder who recommends their appointment. There are cases where directors are employed by shareholders in other capacities in the other shareholders' organisations and receive compensation for their employment. In 2015, the Israeli Securities Authority expressed its opinion in the case of *Oded Sarig*, determining that payment of compensation to a director by a controlling shareholder is not considered a transaction of the public company and therefore not subject to the approvals mechanism determined by the Companies Law.

The court case of *De Lange v Israel Corporation* gave rise to doubts over its legality but has left this matter for further consideration.

Amendment 20 of the Companies Law, passed a number of years ago, enacted the duty to determine that a compensation policy for directors and officers must be approved by a compensation committee, the board and a general meeting by special majority.

Thus, direct compensation of a director by a shareholder, who recommended him or her as a candidate, may create conflict of interests and breach the balance the legislator sought to achieve in Amendment 20 of the Companies Law. In any case, it seems that there is a duty to disclose such payments by the director.

Mandatory bids

13 | Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

In public companies, in order to purchase a control stake, one should do so by a special tender offer. A special tender offer should be carried out when:

- the purchase would result in a single person holding a controlling stake (shares providing 25 per cent or more of the voting rights in the general meeting), if there is no controlling stake in the company beforehand; and
- the purchase would result in the purchaser's share of the holdings rights above 45 per cent of the voting rights in the company, if there is no other person holding over 45 per cent of the voting rights in the company.

Such purchases, as stated above, by means of a special tender offer, shall not apply to:

- purchase of shares by a private placement, provided that the purchase has been approved by the general meeting as a private placementintended to bestow on the offeree a controlling stake if there is no controlling stake in the company beforehand, or as a private placement intended to bestow 45 per cent of the voting rights in the company if the company has no person holding over 45 per cent of the voting rights in the company;
- purchase from a controlling stake holder that would result in a person becoming a controlling stake holder; and
- purchase from a holder of more than 45 per cent of the voting rights in the company that would result in the level of the purchaser's holdings rising above 45 per cent of the voting rights in the company.

As a general rule, shareholders will be deemed to be acting in concert when a written or oral cooperation agreement exists between them on the application of the means of control incorporated in the shares, such as voting rights at general meetings or the right to appoint directors.

In addition, the definition of a 'holding' under the Securities Law provides that when referring to a holding by a company, a subsidiary's holding shall be considered as the holdings of the company; and when referring to a holding by an individual, the individual and members of his or her family, or his or her dependants, are regarded as a single person.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Shareholders are required to disclose their names and holdings in the event of their becoming material holders in the company and thereafter following any changes of their holdings.

A material holder is deemed to be one of the following: a holder of 5 per cent or more of the company's issued share capital or of its voting power, or one who is entitled to appoint one or more of the company's directors or the CEO, or one who serves as a director or CEO of the company, or a corporation that is held by a person holding 25 per cent or more of the issued share capital or of its voting power, or that is authorised to appoint 25 per cent or more of the directors.

Shareholders of banks have additional disclosure requirements.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

In general, there is no duty of disclosure on holdings in derivatives or positions that may make a person a substantial holder in the company, unless he or she is already considered a material holder.

A concert holding of shares constituting 5 per cent or more of the company's issued share capital or of its voting power must be disclosed.

Insider trading

16 | Do insider trading rules apply to activist activity?

The legal provisions concerning the use of insider information apply to shareholder activism.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

The directors are bound by their duty of care and fiduciary duty towards the company and there is no difference in the context of an activist's proposal. Any steps taken by directors in the course of and in relation to shareholder activism, shall not derogate from their duty to act for the benefit of the company.

The director's response to shareholder activism will usually be scrutinised by the business judgement rule (BJR). Judge Ruth Ronen, in the *Altman v Gazit* case, made the BJR applicable to a standstill agreement with an activist, ruling that: 'The desire for a truce among the company shareholders may in some cases be consistent with the benefit of the company and that of its shareholders.'

What do we mean when speaking of 'the company's benefit' that directors and office holders must uphold? Section 11 of the Companies Law provides that

> *the purpose of the company is to act in accordance with commercial considerations for making profits, and as part of these considerations one may take into account, among other matters, the interests of its creditors and employees and those of the public; the company is also permitted to contribute a reasonable sum to a worthy cause even though such a contribution does not stem from commercial considerations, if such is laid down in the provisions of the articles of association.*

A long line of scholars has attempted to get to the bottom of this broad definition, and there are several different views and constructions of how it should be interpreted. The accepted conception in the Israeli legal arena has for many years been that the essence of the company is first and foremost to act in the pursuit of profits, especially for the shareholders. This traditional conception fails to deal with the difficulty in those cases where the interests of the company and its shareholders do not coincide. Israeli case law expressed each one of these interpretations – the one enabling the benefit of the company to be jeopardised for the sake of the shareholders, and the other indentifying the right of the company as a distinct right from the shareholders.

Preparation

18 What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

A company may take a variety of measures to prevent or mitigate potential confrontations with activists.

One of the methods is open communications. A key issue is to maintain an ongoing communication with the company's key investors. Open communication can create a strong trusting relationship with the company management, and can result in support of such investors in case an activist raises allegations against the leaders of the company. Although this may be difficult to maintain and may be inconvenient at times, in the long run, it can be beneficial and minimise crises.

It may be beneficial to be aware of the investors' positions and concerns, including the company's key shareholders (usually the institutional investors) for example, on issues such as the dividend distribution policy, capital investments and executive compensation, and not be first familiarised with them in times of crisis with an activist.

Another method is self diagnosis – identification of vulnerabilities of the company in advance regarding corporate governance and operative aspects. Following its identification, the company should act to mitigate the vulnerabilities. Many companies have updated their corporate governance practices to be in line with market standards. Thus, awareness may keep potential activists away from the company.

Additional method is 'activist thinking'. Here too, similar to self diagnosis, it is important that directors would try to adopt 'activist thinking' and as such would identify and handle existing weaknesses, such as constant evaluation of the company's business strategy and its alternatives. These actions are likely to keep activists away and turn to other companies.

Defences

19 What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

The Israeli Securities Authority objects to extreme controlling entrenchment mechanisms in Israeli public companies, such as staggered board of directors for many years and poison pills of various types, in view of the Israeli Securities Authority's position regarding the importance of maintaining a market of efficient corporate control. The Israeli Securities Authority is not opposed to mechanisms for staggered boards as long as the period set between director replacements does not exceed three years.

It is doubtful that instruments provided in the articles of association – in particular, defence mechanisms against hostile takeover (such as staggered boards, special majority for amending the terms of the articles of association, etc) are appropriate when dealing with activism – since the aim of the activist is usually not to take over the control of the company. Institutional investors as well as their advisory firms also object in principle to controlling entrenchment mechanisms in the articles of association.

There remain less drastic mechanisms to be considered – for instance, amending the articles to hold that a director may only be elected at the annual general meeting and not at a special meeting. This mechanism presents stability to the company and prevents frequent changes in the composition of the board at every whim of the shareholders.

The board of directors is also able to publish a position statement or a response to a position statement of an activist.

In addition, a company can turn to the court to classify the vote of an activist as having a negative personal interest (ie, the shareholder has a personal interest in the failure of the transaction).

Also, some of the companies turn to institutional investors before they convene a meeting to appoint an external director for the purpose of examining whether the candidate proposed by the company will receive the institutional investor support, or that they wish to suggest another candidate.

There are also certain anti-takeover defences determined in the Companies Law - see questions 10 and 13.

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

During the period preceding the general meeting, companies receive proxy votes from shareholders not physically attending the meeting. Shareholders may also vote electronically and the company is accessible to these votes six hours prior to convening the meeting. In addition,

advisory bodies to institutional investors, such as Entropy, provide their position on items on the agenda at a reasonable period in advance, which indicates the manner in which institutional investors receiving the services of the advisory body intend to vote.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

Settlement agreements with activists are becoming more and more common, usually including: a stand still provision for a specified period of time; support of the company's nominees for board membership and support of one or more of the activist's nominees for membership of the company board of directors as long as the activist holds certain minimal ownership position in the company. Settlement agreements between the public company and an activist may be required to be disclosed in accordance with the reporting requirements under the Securities Law and regulations.

A question arises as to the enforcability of settlement agreements in view of the fact that, in such agreements, the company grants significant rights to specific minority shareholders and not to other shareholders. This preference may be found in court to be unlawful or not enforceable.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

Some companies hold regular meetings with investors every few months, either one-on-one meetings or non-deal road shows or conferences or conference calls. Continuous dialogue with investors has become more common in recent years with major investors. For example, there are companies that prior to scheduling a general meeting whose agenda includes the appointment of directors, hold discussions with some of the institutional investors on the identity of the board nominees and their competence to act in the company's interests.

The meetings with the investors vary and include discussions on the company's strategy, and steps for gaining profits as well as corporate governance issues with emphasis on the composition of the board and executive compensation.

23 Are directors commonly involved in shareholder engagement efforts?

Communications with investors are usually conducted by the senior management (eg, CEOs, CFOs) and occasionally the chairman of the board. Usually, independent directors are not involved in the communications with shareholders, unless this has some particular advantage under any specific circumstance.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Companies usually have no disclosure duties regarding their communications with investors and they do not normally report this. Regarding disclosure of a position statement sent by a shareholder to the company – see question 7. Also, it is prohibited to discriminate in the provision of information between different investors, and the practice is to publish investors' presentation on the Stock Exchange and the Israeli Securities Authority reporting website prior to its presentation at an investor's conference.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

There is a prohibition on carrying out transactions with a company's securities based on information not publicly available, which is deemed to be insider information. Companies tend to initiate telephonic conversations or meetings with institutional entity advisory bodies in order to persuade them to provide a professional opinion in support of the items on the agenda of the general meeting. The board is entitled to publish a position statement to investors setting out its position on the agenda items and thus to seek support from the investors. It is not customary for the company to use social media in order to obtain support at the shareholders' meeting.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

Under the Companies Law, a public company must keep a shareholders register and also a register of substantial shareholders. The shareholders register and the register of substantial shareholders shall be open for inspection by any person. It is not clear under the Companies Law whether a company must provide a list of the beneficial owners of its shares.

In addition, one or more shareholders holding 5 per cent or more of the total voting rights in the company, as well as the holder of the said quantity out of the voting rights not part of the holding of the controlling interest in the company, is entitled himself or herself or by an agent on his or her behalf, following the convening of the general meeting, to review at the company's registered office, during normal working hours, the voting cards, the votes via the electronic voting records and the results of the votes.

In addition, shareholders are entitled to review various company documents, including general meeting minutes.

Shareholders also have the right to demand, while indicating the purpose of the demand, to review of any document in the company's possession relating to an operation or transaction requiring the general meeting's approval pursuant to the provision of the Companies Law. The company is entitled to refuse the shareholder's request to review a document in its possession if in its opinion the request was made in bad faith, or if the required documents contain some confidential information, such as trade secret or patent, or if disclosure of the document is not for the benefit of the company.

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

Until recently, institutional investors were concerned about cooperating between themselves regarding activist movements because such cooperation might constitute a restrictive arrangement.

In February 2019, the Competition Authority (formerly the Restrictive Trade Practices Authority) published a draft position statement regarding cooperation by institutional investors. According to the Competition Authority' position, cooperation between institutional investors should not be regarded as a restrictive arrangement if the following conditions are satisfied:

- The cooperation is focused on a particular corporation and on a specific matter under discussion.
- There is no competitive relationship between the activities of the corporation in question and those of the institutional investor.
- Involvement in the cooperation is barred from those whose participation is not essential for appraising the matters over which there is to be cooperation, or in order to attain agreement between the institutional investors; the parties shall only exchange information connected with the cooperation under consideration.

Only relevant information should be forwarded in a manner that minimises any concern of restricting competition between institutional bodies. Following approval of this opinion, it appears that cooperation between institutional investors is about to strengthen significantly, providing them with substantial extra power in activist moves in Israeli public corporations, especially in corporation without a controlling shareholder.

Recently, an interesting activist struggle has been going on in Paz Oil Company. A company with a distributed holdings structure following the sale two years ago by Zadik Bino, formerly the holder of the controlling interest in the company for many years. Paz's financial results were quite good; however, a number of shareholders believed they were insufficient and the company had a problematic balance sheet structure and unsatisfactory corporate governance, which led to a well-publicised activist move by Noked Capital, an Israeli hedge fund managed by Roy Vermus, together with a number of institutional investors. Some of the institutional investors succeeded in appointing Avraham Bigger as a director in Paz on their behalf, to ensure that he will be a dominant chairman who will be able to monitor the dominant CEO of Paz, Yona Fogel. Paz's board met on 20 March 2019 and chose Bigger to become the chairman of Paz following the support of most of the institutional investors who de facto control Paz (without being considered controlling shareholders). Yair Lapidot, co-CEO at Yelin Lapidot – Mutual Funds Management, criticised the chairman election process:

The institutional investors have made an overruling here to the board's search committee following a diligent process, and this is the favourable model that is being welcomed today. Now look what happens, people like Eliezer Shkedi (who served as Commander of the Israeli Air Force and CEO of El-Al), without any interests that joined the company for the purpose of promoting its business, is retiring. This will create endless conflicts between the institutional investors. You do not need all these dramas; huge amounts of energy were spent here; the search committee interviewed dozens of candidates, and finally they told her 'no'.

During the past year, a fascinating struggle has been going on at Mellanox, a semi-conductor firm. In October 2017, the American activist fund Starboard purchased about 11 per cent of Mellanox share capital.

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WITH RAVED, MAGRISO, BENKEL & CO.

Amir Shachar
a.shachar@shibolet.com

Museum Tower Office
4 Berkowitz St
Tel Aviv 6423806
Israel
Tel: +972 3 7778333
Fax: +972 3 7778444
www.shibolet.com

The fund conducted a well-publicised campaign against the management and board of Mellanox, asserting that the company was underpriced because of its low operating profitability, and demanding members of the board be replaced. Following a few months of mutual moves by the company and the activist fund, the parties reached a settlement regarding appointment and replacement of some of the members of the Mellanox board and setting profitability targets. This activist campaign led to a more profitable and efficient operation, increasing significantly the share price of Mellanox. In March 2019, Mellanox was acquired by Nvidia for US$ 6.9 billion in cash. Starboard bought Mellanox shares for approximately US$250 million in late 2017 and sold them for approximately US$525 million.

Another American fund operating in the Israeli capital market in the past year is Elliott, belonging to Paul Singer. The fund held about 5 per cent of the share capital of Israel leading telecommunications service provider Bezeq and demanded changes to the Bezeq board, including the immediate resignation of all directors that had been under investigations of the Israeli Securities Authority or had connections with Eurocom – the controlling shareholder of Bezeq in the days of Shaul Elovitch. Resulting from the funds moves, and moves of institutional investors and their advisory bodies, none of these directors now serve on the board of Bezeq. The fund also tried to influence Bezeq to execute a repurchase of Bezeq shares; however, this attempt failed.

Japan

Yo Ota, Ryutaro Nakayama and Shigeru Sasaki
Nishimura & Asahi

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The Companies Act and its relevant ordinances provide for the rights of shareholders with regard to the company and its organisation, such as the right to make a shareholder proposal or initiate a derivative suit against directors. The rights stipulated in the Companies Act are, in principle, of a civil nature and enforced through court rulings.

The Financial Instruments and Exchange Act (FIE Act) and its relevant orders and ordinances regulate or provide for:

- the disclosure obligations of companies whose securities are widely held;
- the rights of investors to sue the company or its related parties;
- the rules regarding a tender offer (TOB);
- the disclosure obligations of an investor with large shareholdings;
- the rules protecting market fairness, such as prohibitions against market manipulation and insider trading; and
- the rules regarding a proxy fight.

The FIE Act has both civil and administrative aspects. It is therefore enforced through court rulings and administrative actions by the relevant authorities, such as the Financial Services Agency and the Securities and Exchange Surveillance Commission. In some cases, criminal sanctions may be imposed for certain violations.

Both the Companies Act and the FIE Act are legislated and amended by the Diet, while relevant Cabinet orders and ordinances are enacted by the Cabinet or by various ministries or agencies, such as the Financial Services Agency, as the case may be.

Securities exchange rules and guidelines also regulate disclosures by listed companies, and their communications with investors. While such rules and guidelines are not enforced through court rulings or administrative procedures, securities exchange regulatory entities may impose various sanctions against a violating company, including a suspension of transactions of the company's shares on the securities exchange, a designation as a security on alert, a monetary penalty for a breach of the listing contract, submission of an improvement report, and, in extreme cases, delisting.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Activists' campaigns have been very frequent recently. Based on a media reports, activist held shares in listed companies worth as much as 1.6 trillion yen in market values. Some funds try to have a dialogue with management to improve the governance structure, management plan, or financial structure of the targeted company. They will sometimes launch a formal shareholder proposal at a general shareholders' meeting to elect outside directors or to increase dividends. As such proposals are generally in line with other shareholders' common interests, and due to the fiduciary duty of financial institutions and non-activist type of funds as shareholders complying with the Stewardship Code (which may also be applied if a shareholder voluntarily chooses to accept the Stewardship Code and does not have any legally binding power), it is not uncommon for such proposals to attract general shareholder support even without intensive proxy campaigning.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

Shareholder activism has been mostly viewed negatively, as the activities of activists are sometimes deemed short-termism, which is criticised in the Stewardship Code and the Corporate Governance Code. However, in some instances, those views may change if activist shareholders make proposals that are reasonable or constructive for mid-term or long-term investors. While there is little observable bias among the industries targeted by activist shareholders, on an individual company level, one or more of the following factors often apply to the targeted listed companies:

- low price-to-book ratio;
- excess reserved cash or cash equivalents;
- management scandals or inefficient management;
- status as a conglomerate; and
- status as a listed subsidiary.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

While there are some individual activist shareholders who make shareholder proposals or, in some instances, bring a lawsuit against the targeted company, most activist shareholders of Japanese companies are financial funds. While the boundaries are not so clear, such activist funds can be categorised into two types.

The first are 'aggressive' or 'dogmatic' activists who seek short-term returns by putting pressure on the company's management in various ways. They criticise the existing management's plans or skills or, as the case may be, any management scandals in order to put pressure on management, via either private or public methods such as media appeals, proxy campaigns or partial tender offers. Although their arguments are often too dogmatic and myopic to attract the support of other shareholders, in order to avoid wasting management resources and damaging the company's reputation, management will sometimes

compromise with an activist's proposal or support an exit of an activist's investment.

The second are 'soft' activists. They would prefer to have a dialogue with management to improve the governance structure, management plan or financial structure of the targeted company. They will sometimes launch a formal shareholder proposal at a general shareholders' meeting to elect outside directors or to increase dividends. As such proposals are generally in line with other shareholders' common interests, it is not uncommon for such proposals to attract general shareholder support even without intensive proxy campaigning.

The third type are 'M&A activists'. They invest in a company that is the target of or the parties of M&A transactions. Such funds do not necessarily object to the transaction itself but demand, as a minority shareholder, more favourable conditions for the transactions. With the favourable conditions, these funds then exit.

In addition to those types, in 2016, another type of activist appeared in the Japanese market. However, those funds did not become the mainstream of shareholder activism in the Japanese market. Funds have started targeting companies whose shares are, in a fund's opinion, overvalued. First, the fund shorts the target shares by borrowing the shares from lenders, then the fund makes a public report to the effect that the target shares are overvalued. After the share price drops, the fund then acquires the shares and returns them to the lenders. Because of the nature of their strategy, this type of activist typically does not make shareholder proposals.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

Traditionally, activist shareholders in Japan have demanded that the targeted companies increase dividends or buy back shares. Another common request by activist shareholders is the introduction of or increase in the number of outside directors. On the contrary, US-based activist shareholders have sometimes requested that Japanese companies make drastic business divestures.

Traditional proposals for the increase of dividends or share buybacks are still made but activist shareholders have recently been campaigning more often about governance concerns. In addition to proposals regarding outside directors or opposition to a company's slate, activist shareholders, especially US-based activist shareholders, have campaigned for divestitures of cross-held shares (or *mochiai*). In addition, certain US-based activist shareholders have conducted campaigns to raise the TOB prices in some Japanese listed companies that were the targets in friendly M&A transactions by way of the TOB.

On the other hand, some individual activists tend to focus more on social issues, such as the abolition of nuclear power plants.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

In most cases, activist shareholders try to negotiate with management privately. Aggressive activist shareholders sometimes disclose their proposals or requests publicly without any private negotiation, in order to put pressure on management.

With respect to general shareholders' meetings, which must be held at least annually, activist shareholders submit shareholder proposals as mentioned in question 6, and sometimes wage proxy fights to pass their proposals. Such shareholder proposals include proposals to appoint one or more outside directors. Another form of proxy fight is opposing a company's slate. Activist shareholders have rarely been successful in gaining mainstream investor support of such proxy fights. However, in 2017, Kuroda Electric's general shareholders' meeting approved the only candidate on the dissident slate.

In addition to the above strategies, while it is not so common, activist shareholders can also threaten to launch a TOB for target shares. Some activists use the threat of a lawsuit against the targeted company or its management. However, regulations on giving benefits to shareholders prohibit any person, including activists, from demanding money or any form of benefit, including a company buy-back of activist shares, in return for withdrawing their shareholder proposals or requests.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

In principle, in a listed company, a shareholder who satisfies certain requirements may propose a matter to be discussed at a general shareholders' meeting up to eight weeks prior to the meeting (section 303, the Companies Act). The eligible shareholder must possess 1 per cent or more of the issued and outstanding shares, or 300 or more voting rights, for more than six months before submitting the proposal. The same shareholding minimum and shareholding period apply if a shareholder demands that the company describe the specific content of a proposal in the convocation notice of a general shareholders' meeting at the company's cost. A company may limit the number of words of the proposal description in accordance with its internal rules and procedures for managing shares. If the proposal violates any law or the articles of incorporation of the company, or if a substantially similar proposal was not supported by more than 10 per cent of the voting rights of all shareholders during the three-year period immediately preceding the proposal, the company may decline to include the proposal in the convocation notice.

If a shareholder does not demand the inclusion of its proposal in the convocation notice, there are no shareholding minimums or shareholding period requirements, and every shareholder who has a voting right may submit a proposal at any time. However, a proposal is not permitted if it violates any law or the articles of incorporation of the company, or if a substantially similar proposal was not supported by more than 10 per cent of the voting rights of all shareholders during the three-year period immediately preceding the proposal.

The above rules apply to every shareholder regardless of the nature of the shareholder.

Owing to several incidents, the Ministry of Justice, which drafts the Companies Act and its amendments, has tried to submit a bill to defend against abusive proposals, by limiting the number of shareholders' proposals and prohibiting certain proposals that mainly disparage others or disturb the shareholders meeting.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Shareholders may nominate directors who are not on the company's slate. Nominations are considered to be shareholder proposals. See question 7 for the appropriate procedures.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

For a listed company, a shareholder who has more than 3 per cent of all voting rights during the six-month period immediately preceding the

proposal may call an extraordinary shareholders' meeting (section 297, the Companies Act).

If the company does not send the convocation notice promptly, or if the convocation notice does not indicate that the extraordinary shareholders' meeting will be held within eight weeks of the shareholder's demand, the demanding shareholder may call, by himself or herself on behalf of the company, an extraordinary shareholders' meeting with court approval (section 297, the Companies Act). The courts must approve such convocation unless circumstances indicate that the shareholder is merely abusing his or her rights to create a nuisance or other similarly irrelevant purposes.

If shareholders unanimously approve a proposal by written consent in lieu of a meeting, such approval is deemed to be the equivalent of a resolution of a shareholders' meeting (section 319, the Companies Act). If the consent is not unanimous, the consent is not equivalent to a resolution. In listed companies, each shareholder may exercise its voting rights in writing or through a website without physically attending the meeting.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Shareholders may bring derivative actions (section 847, the Companies Act). Although it may be theoretically possible to bring a tort claim against the company in some instances, the derivative actions are the main type of litigation shareholders initiate.

Shareholders who have continuously held shares for more than six months may demand that the company sue its directors (and other officers, if applicable). If the company does not file the lawsuit within 60 days of the demand, the shareholders may bring a derivative action on behalf of the company. The shareholders of the parent company may also file a derivative suit against directors (and officers, if applicable) of wholly owned subsidiaries of the parent company (ie, a double or multiple derivative suit) if such subsidiary does not file the lawsuit within 60 days of the demand against the subsidiary by the parent company's shareholders.

The company cannot strike down the lawsuit by itself even if it is an abusive action by a shareholder. However, if it is abusive, in theory, the company may pursue a tort claim against the shareholder and request damages. In order to ensure that the company may recover damages if a derivative action is found to be abusive, the court may order the shareholder to place a certain amount in escrow prior to the start of a derivative action (section 847-4, paragraph 2, the Companies Act).

Japan does not have class action lawsuits similar to those in the United States, and a person cannot file a multi-plaintiff litigation without obtaining the approval of each plaintiff. Although a new type of 'consumer litigation' was introduced on 1 October 2016, securities transactions may be outside the scope of this new type of litigation, as tort claims under the new type of litigation are limited to claims based on the Civil Code of Japan, even though litigation in Japan regarding securities transactions belongs to the wider category of tort claims.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

It is not commonly considered that the shareholders owe fiduciary duties to the company. The listing rules require intensive disclosures with respect to the transactions between the parent company and its listed subsidiary.

Compensation

12 May directors accept compensation from shareholders who appoint them?

The Companies Act is silent on this issue. However, a director must act for the best interests of the company. If an individual shareholder directly compensates a director, the payment is treated as a gift, not salary, for tax purposes. In addition, if a director acts for the benefit of any specific shareholder(s) instead of for the benefit of the company due to being directly compensated by such shareholder, it may be a criminal breach of trust that violates regulations on giving benefits to shareholders.

However, some subsidiaries of listed companies are also listed companies themselves, and directors of such subsidiaries are often employees seconded or dispatched from their parent companies. Under such circumstances, the compensation a director receives as an employee of the parent company may inevitably appear to be compensation for acting as a director of a subsidiary. Even in such circumstances, the director must act for the benefit of the subsidiary, not for the parent company.

Mandatory bids

13 Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

The FIE Act requires a mandatory TOB be conducted when a party acquires shares from off-market trading and consequently holds one third or more of all voting rights. If multiple purchasers act in concert, the above threshold, one-third, is determined in aggregate. Therefore, if the aggregate shareholding ratio of shareholders acting in concert exceeds one-third and such shareholders intend to acquire additional shares in an off-market transaction, they must make a TOB. This requirement, however, does not apply to share acquisitions in the market. In addition, even a mandatory TOB does not necessarily result in the acquisition of all the shares of the targeted company, and the purchaser may make a capped TOB.

Under the FIE Act, persons having agreed (i) to jointly acquire or transfer the shares, (ii) to jointly exercise voting rights or other rights as shareholders, or (iii) to transfer or accept transfer of the shares between them after the planned acquisition are deemed to be acting in concert. In addition, those who (i) have certain family relationships or capital relationships (in latter case, including the entities), or (ii) serve as an officer of the acquiring company or other certain company that has certain capital relationships with the acquiring entity, are deemed to be acting in concert.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

The FIE Act requires a shareholder of a listed company to file a report of the possession of a large volume of shares within five business days after the shareholding ratio of the shareholder exceeds 5 per cent. When reporting the possession of a large volume of shares, the purpose of the investment has to be disclosed. If the shareholders intend to make certain managerial proposals and shareholders proposals, such intention has to be disclosed.

If multiple persons acquire shares of the same company in concert, or if multiple persons agree on the exercise of voting rights, the threshold is determined based on the aggregate of those persons' shares, but determining whether multiple persons are acting in concert is difficult and is not necessarily enforced.

Certain institutional investors, including banks, broker-dealers, trust banks, and asset management companies, may file the report based on the ratio on the record date, which in principle is set once per two weeks if the investor holds 10 per cent or less and does not intend to act to significantly influence the operation or management of the issuer company.

A violation of the reporting obligation may result in an administrative monetary penalty.

Additionally, in certain transactions where an acquiring company and a targeted company are considered to be large by industry standards, antitrust laws require a prior filing, including disclosure of the shareholding ratio, and mandate an appropriate waiting period. Further, the Japanese Foreign Exchange and Foreign Trade Control Law requires non-Japanese investors to make the filing prior to acquiring 10 per cent or more shares of listed companies in certain industries designated by the Japanese government as vital to national security, public order, or the protection of public safety. Such industries include, among others, electric power, natural gas, telecommunications, broadcasting, and railways.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

To determine the shareholding ratio for a report of the possession of a large volume of shares, shares obtained by certain types of stock lending and certain share options have to be aggregated. Though the long positions of total return swaps are generally not included, certain types of total return swaps conducted for purposes other than pure economic profit or loss must also be aggregated. Consequently, in some cases, activists have not filed a report of the possession of a large volume of shares even though they purported to 'own' more than 5 per cent and have made certain demands or held certain conversations as large shareholders.

Insider trading

16 | Do insider trading rules apply to activist activity?

Trading by an activist is regulated by the insider trading rules. If the activist is aware of any material non-public information of the company through the activist activity, market trading by the activist is prohibit until the information becomes public. The mere fact that the activist made the shareholders' proposal may not be material non-public information, depending on the discussions with the company, but there may be material non-public information.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

In general, a director's duty with respect to an activist proposal is similar to other board decisions; namely, the business judgement rule. Unless there is a conflict of interest between the company and the directors, and unless there is a violation of laws or the articles of incorporation of the company, the courts generally respect the wide discretion of the board, assuming that the board made a reasonable decision that duly recognised the applicable facts and circumstances. However, even under the business judgement rule, Japanese courts may sometimes carefully scrutinise the context and situation surrounding the board's decision. It has thus far been understood that no controlling shareholder owes any fiduciary duty to minority shareholders.

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

As activist shareholders have enhanced their presence in Japanese businesses, we generally advise our clients to periodically check the shareholders' composition and improve their governance structures, business plans or financial structures, and recommend that they engage in proactive communication with their shareholders.

Defences

19 | What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Based on the report published by the Tokyo Stock Exchange in March 2017, more than 12 per cent of companies listed on the Tokyo Stock Exchange have adopted the Japanese rights plan or 'large-scale share purchasing policies', even though the ratio has been gradually decreasing (the ratio is higher among larger market-cap companies in comparison). Under such a plan, a company implements procedures in advance that a potential raider must follow, although the company does not issue rights or warrants (unlike 'poison pills' in the United States). If a potential raider crosses the threshold (typically, 20 per cent) without complying with the procedures, or a potential raider is recognised as an 'abusive raider', new shares will be issued and allocated to all shareholders other than the violating raider; thus, the raider's shareholding will be diluted.

Other than such a plan, structural defences such as dual capitalisation are rarely possible, although one company (Bull-Dog Sauce) was successful in this, because the defence measure was fair and reasonable. Though Bull-Dog Sauce had not adopted the rights plan, and the anti-takeover defence measures in the case were adopted after the raider announced its intent to launch a TOB, the Supreme Court stated in obiter that such a rights plan had a net positive effect, as it heightened the predictability of the outcome of a takeover. The Supreme Court also followed this logic in the guidelines for defence measures against hostile takeovers issued by the Japanese Ministry of Economy, Trade and Industry.

During 2017, there were no changes in the laws and regulations or court rulings to limit the anti-takeover defences available to a company

particularly because of the listing rules. In addition, as the term of office of a director at a Japanese listed company is one or two years depending on its governance structure, a staggered board is not an effective measure in practice.

While there are few cases where the validity of the rights plan or anti-takeover defence measures has been tested, in the Bull-Dog Sauce case, the Supreme Court recognised the validity of an anti-takeover defence (similar to a poison pill in the United States) implemented by the target.

Proxy votes

20 | Do companies receive daily or periodic reports of proxy votes during the voting period?

Trust banks that act as standing agents receive voting forms from shareholders. Consequently, in practice, a company may receive early voting ratio and other information during the period for sending back voting forms (ie, after the convocation notice but before the due date of the voting forms). The company is not obliged to disclose any information it receives from the voting forms prior to the date of the general shareholders' meeting. During a proxy fight, however, a company does not have any way of determining how many proxies an opposing shareholder will receive.

Settlements

21 | Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

As mentioned in question 10, 'soft' activists would prefer to have a dialogue with management to improve the governance structure, management plan, or financial structure of the targeted company. Although they will sometimes launch a formal shareholder proposal at a general shareholders' meeting, the company sometimes agrees on the proposal without the proxy campaign.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 | Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

While organised engagement among activist shareholders is not common, when an activist shareholder launches a campaign, other activist shareholders may support the campaign. Consequently, engagement efforts tend to be public and formal. Even during a public campaign, the company may choose to compromise by accepting the activist's proposal or presenting the proposal during the shareholders' meeting as the company's proposal.

23 | Are directors commonly involved in shareholder engagement efforts?

While the Japanese Corporate Governance Code recommends that directors take a leading role in engaging with shareholders, in most cases, management or the executive team is in charge of shareholder engagement efforts. Executive directors are sometimes directly involved in shareholder engagement, but it is at the company's discretion.

NISHIMURA & ASAHI

Yo Ota
y_ota@jurists.co.jp

Ryutaro Nakayama
r_nakayama@jurists.co.jp

Shigeru Sasaki
s_sasaki@jurists.co.jp

Otemon Tower, 1-1-2 Otemachi
Chiyoda-ku
Tokyo 100-8124
Japan
Tel: +81 3 6250 6200
Fax: +81 3 6250 7200
www.jurists.co.jp

Disclosure

24 | Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Under the Japanese Corporate Governance Code, the board of a listed company must determine and approve a corporate governance policy that facilitates constructive dialogue with shareholders, and disclose the policy in a corporate governance report that must be filed under section 419 of the Securities Listing Regulations. Individual communications need not be disclosed.

Through the amendment to the FIE Act and new Cabinet orders and ordinances that were implemented from 1 April 2018, listed companies are required to make equal disclosure to a certain degree to all shareholders. The new regulation is similar to Regulation FD in the United States, rather than the EU Market Abuse Regulations. Even under the new regulations, a listed company may make selective or unequal disclosure if the recipient owes a non-disclosure obligation and is prohibited from making a transaction of the company's securities. If disclosure to a shareholder, investor, or other third party is not exempted and is intentionally made, the company must make public disclosure at the same time as the disclosure to such third party. If the disclosure is not intentionally made, the company must make public disclosure immediately after the disclosure to such third party. The company may make public disclosure through the Electronic Disclosure for Investors' Network (EDINET) run by the Financial Services Agency, TD-net(the electronic disclosure system of the Tokyo Stock Exchange) or its corporate website.

In addition to the above fair disclosure regulation, the disclosure of insider information to specific shareholders under certain circumstances may result in a violation of insider trading regulations.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

Regulations on proxy solicitations or Japanese proxy rules apply to both companies and shareholders when they solicit proxies (section 194, the FIE Act; section 36-2 to 36-6, Enforcement Order of the FIE Act; and Cabinet Office Ordinance on the Solicitation to Exercise Voting Rights of Listed Shares by Proxy). The regulations set forth certain requirements on the proxy, and also require that certain information be provided to the shareholders during a proxy solicitation. However, if the same information is disclosed in the reference documents that are typically enclosed with the convocation notice of a shareholders' meeting for which proxies are solicited, those who solicit the proxies (the company or the shareholders) do not have to separately provide the above-mentioned required information. Further, if a company solicits proxies, offering certain economic benefits to shareholders to facilitate favourable voting results may violate regulations on giving benefits under the Companies Act. Currently, social media platforms (such as Twitter and LinkedIn) are not commonly used as communication tools during campaigns between targeted companies and activists.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

A shareholder on the shareholders' list may request access to the shareholders' list (section 125, paragraph 2, the Companies Act). The company may reject such a request on certain grounds, including:

- if the request is made for purposes other than exercising general shareholder rights;
- if the request is made with the purpose of interfering with the execution of the operations of the company or prejudicing the common benefit of the shareholders;
- if the request is made in order to report facts obtained through a request to a third party for profit; or
- if the requesting shareholder reported facts obtained through a prior request to a third party within two years (section 125, paragraph 3, the Companies Act).

The shareholders' list in a listed company only records nominee shareholders, and the beneficial owners are not recognised by the shareholders' list.

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

On 5 December 2018, the extraordinary general shareholder's meeting of Alpine Electronics, one of the major manufacturers of car navigation systems, approved a share-for-share exchange between Alpine and Alps Electric Co. In this transactions, two funds were in the spotlight; Elliott and Oasis Management. While Elliott is not reported to be an activist in Japanese market, it is famous in the United States. Oasis Management is reported to be conducting activist activity in Japan. Oasis once successfully caused Panasonic to conduct a TOB in its acquisition of the whole shares of its listed subsidiary at that time (current Panasonic Homes Co). Oasis made an aggressive engagement with Alpine, including the shareholder proposal to increase dividends, and opposed the exchange ratio, as it was low. It is reported that Oasis intended to achieve another success in the Alps-Alpine transaction. On the other hand, Elliott acquired shares both in Alpine and Alps, and finally supported the transaction. During the proxy, it was reported that the transaction was a proxy fight between two funds.

As written in the articles, shareholder activism has not been supported so much in the Japanese market; the listed companies have to take care about shareholder activism. It is reported, based on a trust bank's research, that, in 2018, 66 activist funds increased their Japanese investment, while 33 funds decreased. The shareholder activism may continue to be a hot topic in the Japanese market.

Luxembourg

Margaretha Wilkenhuysen
NautaDutilh Avocats Luxembourg

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

Luxembourg's main statutes on corporate governance include the 10 August 1915 act on commercial companies (the Companies Act), which was revamped in 2016 in order to modernise Luxembourg corporate law, the Market Abuse Regulation and the Act of 24 May 2011 (the Shareholder Act).

Shareholder rights and governance in Luxembourg are statute-based, consisting primarily of the Civil Code, the Companies Act and, for listed companies, the Shareholder Act and the rules and regulations of the Luxembourg Stock Exchange (LuxSE).

The Shareholder Act came into force on 1 July 2011. It implemented Directive 2007/36/EC on the Exercise of Certain Rights of Shareholders in Listed Companies, aiming to increase shareholders' activism and setting out a number of shareholders' rights. This Shareholder Act is subject to further amendment as a result of the transposition into Luxembourg law (expected mid 2019) of the Second Shareholders' Rights Directive. The Second Shareholders' Rights Directive, which must be implemented in Luxembourg law by June 2019, sets out rules on, inter alia, 'say on pay', identification of shareholders, transmission of information and transparency of institutional investors, asset managers and proxy advisers.

As a supplement to the general statutory law, the LuxSE's 10 Principles of Corporate Governance (the LuxSE Principles), as modified in October 2009 and revised in March 2013 (third edition) and December 2017, provide guidelines on best practice in corporate governance for all companies listed on the LuxSE. Luxembourg companies listed abroad often find inspiration in these LuxSE.

Moreover, in 2007, Luxembourg implemented Directive 2004/39/EC on Markets in Financial Instruments, effective at that time (MiFID), introducing new provisions on transparency for shares and transaction reporting. In addition, as of the entry into force of the EU Regulation on Markets in Financial Instruments, the provisions of the regulation are directly applicable in Luxembourg.

Companies whose shares are admitted to trading on a regulated market in a member state of the EU, including Luxembourg, may also be subject to the Act dated 19 May 2006 on Takeover Bids, as amended (the Takeover Bid Act). The Takeover Bid Act notably provides for minority shareholder protection, the rules of mandatory offers and disclosure requirements.

In 2008, the Transparency Directive (Directive 2004/109/EC) was transposed into Luxembourg legislation through the Act of 11 January 2008 (the Transparency Act).

A breach of certain statutory provisions of the Companies Act and, for listed companies, the Shareholder Act qualifies as a criminal offence, although prosecution is rare.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

There are very few publicly available examples of shareholder activism in Luxembourg listed companies. The most prominent example was the takeover of Arcelor by Mittal, which was only finally made possible following the pressure of the shareholders. This concrete example, however, is already more than 10 years old, since the takeover took place in 2006.

Furthermore, Deminor, a firm that is actively engaged in shareholder activism by representing minority shareholders and enforcing their claims accordingly, refers to a couple of Luxembourgish companies on its website. Their names are redacted for obvious disclosure reasons, which makes it almost impossible to identify the companies concerned, but it is quite likely that they already have or will target Luxembourg listed companies.

On a side note, Luxembourg host a number of funds that invest in companies worldwide and are active as shareholders in these entities. As an example, Active Ownership is a fund, based in Luxembourg, that managed to replace certain members in the supervisory board of STADA.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

Luxembourg and EU company law reforms introduced new or strengthened shareholder rights around the turn of the 21st century, There is a trend in Luxembourg law for more transparency, accountability and increased shareholder rights, especially in listed companies. In addition, minority shareholders have additional rights further to the changes to the Companies Act in 2016. It is hard to predict whether these changes will lead in practise to more public campaigns led by activist shareholders or not. It is certain that boards will, however, have to take into account the potential involvement and action from their shareholders, including minority shareholders. See also 'Update and trends'.

In Luxembourg, no particular industries are more or less prone to shareholder activism. Activist campaigns against 'national champions' tend to face more backlash from the general public and politicians.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

Deminor, a firm that is actively engaged in shareholder activism by representing minority shareholders and enforcing their claims accordingly, refers to a couple of Luxembourg companies on its website. Their names are redacted for obvious disclosure reasons, which makes it almost impossible to identify the companies concerned, but it is quite likely that they already have or will target Luxembourg listed companies.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

Activist campaigns would typically be focused on a company sale or break-up, bumpitrage or return of capital. Long-term institutional investors tend to focus more on environmental, social and governance (ESG) topics and executive compensation or say-on-pay.

Factors that tend to attract activists' attention include announced or potential M&A events, low leverage or strong cash positions, as well as perceived corporate governance issues, underperformance and inflated executive pay.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

Depending on the type of activist, its goals and the company's takeover defences, activists may use a number of different tactics to pursue their objectives, such as:

- privately engaging through informal discussions or 'dear board' letters (the starting point of most activist campaigns and the preferred tool of most institutional investors);
- publicly criticising a company's strategy, governance or performance or calling for a sale, break-up, return of capital or increased offer price ('bumpitrage');
- short-selling stock and starting a public campaign to drive down stock prices;
- stakebuilding to build up pressure on the boards and signal seriousness;
- partnering with a hostile bidder;
- participating in and voting at general meetings;
- orchestrating a 'vote-no' campaign;
- making a shareholders' proposal or requesting an EGM be convened; or
- initiating litigation

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

Shareholders representing individually or collectively at least 5 per cent of a Luxembourg company's capital request, for listed entities falling within the scope of the Shareholder Act or 10 per cent for the other entities, as the case may be, have the right to amend a notice to the shareholder meeting and add additional items on the agenda. The company may refuse to put an item on the agenda as a voting item (rather than a discussion item), if it concerns a matter that falls outside the power of the general meeting. In addition, shareholders representing 10 per cent of a company's share capital may force the board to postpone a general meeting of shareholders for a period of up to four weeks.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Even if director nomination is typically made via the company's nomination committee, any shareholder holding at least 5 per cent for listed entities falling within the scope of the Shareholder Act or 10 per cent for the other entities, as the case may be, has the right to amend a notice to the shareholder meeting and add the nomination of directors for election.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Shareholders representing individually or collectively at least 10 per cent of a Luxembourg company's capital (or such lower percentage as prescribed in the company's articles) may request of the the board that a general meeting be convened. The request must set out in detail the matters to be discussed. If the board has not taken the steps necessary to hold a general meeting within one month (if the company's shares are not listed on a regulated market within the EEA) of the request, the requesting shareholders may be authorised by the district court in preliminary relief proceedings to convene a general meeting provided that they have a reasonable interest in holding the meeting.

No written resolutions can be taken.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Shareholders can seek nullification of corporate resolutions (arguing, for instance, that the resolution is contrary to the company's interest) or bring wrongful act claims against companies or its directors (arguing that a particular conduct of the company or its directors constituted a tort against the claimant).

Derivative actions do not exist under Luxembourg law. Luxembourg law does not provide for class actions.

During the annual general meeting, the shareholders can question the board on all aspects of the company's management, accounting and so forth throughout the year, and may withhold the granting of discharge.

The right of shareholders to ask questions during the meeting and to receive answers to their questions is legally enshrined.

Under the Shareholder Act, in addition to the right to ask questions orally during a meeting, shareholders may have the right to pose written questions about the items on the agenda before the meeting is held. If provided for in a company's articles of association, questions may be asked as soon as the convening notice for the general meeting is published. The company's articles of association will furthermore provide the cut-off time by which the company should have received the written questions.

Apart from several specific circumstances (eg, in the case of confidential information), the company must answer any questions addressed to it. Should several questions relate to the same topic, the company may publish a detailed questions and answers document on its website, in which case the chair should draw the shareholders' attention to the publication.

The Companies Act also allows shareholders to submit questions to management outside a meeting. Any shareholder representing at least 10 per cent of the company's share capital or voting rights, or both, can ask the board of directors or management body questions about the management and operations of the company or one of its affiliates, without the need for extraordinary circumstances. If the company's board or management body fails to answer these questions within one month, the shareholders may petition, as in summary proceedings, the president of the district court responsible for commercial matters to appoint one or more independent experts to draw up a report on the issues to which the questions relate.

Certain matters must also be reported to the shareholders, such as any director's conflict of interest relating to voting on a resolution.

While the concept of discovery does not exist under Luxembourg law, a party with a legitimate interest may submit a motion to the court demanding the production of specified documents pertaining to a legal relationship to which the requesting party or its legal predecessor is a party.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 | Do shareholder activists owe fiduciary duties to the company?

Under Luxembourg law, shareholders may, in principle, give priority to their own interests.

Compensation

12 | May directors accept compensation from shareholders who appoint them?

There is no Luxembourg law that prohibits a director of a Luxembourg company from accepting compensation from a shareholder who nominated or appointed him or her. Irrespective of whether a director is nominated, appointed or compensated by a specific shareholder, Luxembourg corporate law requires all directors to be guided by the corporate interests of the company and its business in performing their duties and to consider with due care the interests of all stakeholders. To the extent that any such compensation creates, in respect of a particular board matter, a direct or indirect personal interest for such director that conflicts with the interests of the company and its business, the director may not participate in the deliberations and decision-making of the board on such matter.

Mandatory bids

13 | Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

The Luxembourg mandatory offer rules only apply to Luxembourg public companies whose shares or depositary receipts for shares are listed on a regulated market within the EEA. Pursuant to the CSSF and subject to limited exemptions, a mandatory offer requirement is triggered if a person, or a group of persons acting in concert, obtains the ability to exercise at least 33.3 per cent of all outstanding voting rights in a company (predominant control).

Concert parties shall mean natural or legal persons who cooperate with the offeror or the offeree company on the basis of an agreement, either express or tacit, either oral or written, aimed either at acquiring control of the offeree company or at frustrating the successful outcome of a bid.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Pursuant to the Transparency Act, any person who acquires or disposes of shares or voting rights of a Luxembourg company whose shares are listed on a regulated market within the EEA, must forthwith (generally, the next trading day) notify the issuer of the proportion of voting rights of the issuer held by the shareholder as a result of the acquisition or disposal where that proportion reaches, exceeds or falls below the thresholds of 5, 10, 15, 20, 25, 33.3, 50 and 66.6 per cent. It is not needed to include shareholders intentions.

At a few listed Luxembourg companies, the articles of association impose additional notification obligations on shareholders.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

Depositary receipts for shares are taken into account for purposes of calculating the percentage of capital interest and voting rights.

For purposes of calculating the percentage of capital interest and voting rights held by a person, shares and voting rights held by the person's controlled entity, by a third party for the person's account or by a third party with whom the person has concluded an agreement to pursue a sustained joint voting policy, are taken into account.

Insider trading

16 | Do insider trading rules apply to activist activity?

Yes, the insider rules apply with respect to Luxembourg companies whose shares or other financial instruments are listed on a regulated market within the EEA. No person may:

- engage or attempt to engage in insider dealing;
- recommend that another person engage, or induce another person to engage, in insider dealing;
- unlawfully disclose inside information; or
- engage, or attempt to engage, in market manipulation.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

Luxembourg corporate law requires all directors to be guided by the corporate interests of the company and its business in performing their duties. If the company has a business, the interests of the company generally are particularly defined by the interest of promoting the sustainable success of the company's business (ie, a focus on long-term value creation). Boards must weigh all relevant aspects and circumstances and shall consider with due care the interests of all stakeholders, including shareholders, employees, creditors and business partners. Boards have a lot of discretion on how to weigh the various stakeholders' interests against each other, although the duty of care may require boards to prevent unnecessary or disproportionate harm to the interests of specific stakeholders. The board is responsible for determining and implementing the strategy of the company.

Responding to an unsolicited approach or activist proposal seeking to change the company's strategy (including by means of efforts to change the board composition) forms part of the company's strategy and, as such, falls within the domain of the board. There is no shift of

fiduciary duties: the directors must continue to act in the best interests of the company and its business with a view to long-term value creation, taking into account the interests of all stakeholders. Boards should ensure that they have all relevant information to make an informed decision and the proposal should be carefully reviewed, without bias, and assessed against all available alternatives. Shareholders do not have to be consulted prior to the company's response; the board is (retrospectively) accountable to the shareholders.

Preparation

18 What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

Although the absolute number of activist campaigns in Luxembourg is limited, no company is immune to activism and preparedness is key. While recommended advance preparations depend on the specifics of the company, a few useful preparations are:

- continuously monitoring market activity, financial performance (particularly relative to peers) and the company's industry and competitors;
- setting up a small defence team of key directors/officers plus legal counsel, investment banker and public relations firm that meets periodically;
- 'thinking like an activist', routinely assessing the company's strengths and weaknesses and its takeover defences and exploring available strategic alternatives (consider red teaming);
- building relationships and credibility with shareholders and other stakeholders before activists emerge and maintaining regular contact with major shareholders, the marketplace generally and key stakeholders; and
- communicating clearly and consistently on ESG/corporate social responsibility matters, the company's long-term strategy, its implementation and the progress in achieving it.

Defences

19 What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Some listed Luxembourg companies have adopted one or more structural takeover defences, often in their articles of association. Examples include:

- priority shares with certain control rights; or
- listing of depositary receipts for shares rather than the shares itself.

In addition, Luxembourg companies may use a variety of other tactics such as:

- engaging with shareholders and other stakeholders (eg, convince major shareholders with compelling long-term plans, mobilise employees and customers);
- exploring strategic transactions that make the company a less desirable target;
- issuing new shares (under existing authorisations) or selling treasury shares to a friendly third party (white knight); or
- issuing bonds with a mandatory redemption at a higher value in case of a change of control.

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

It depends on the listing venue. Luxembourg companies with a US listing often (choose to) receive regular updates on the vote tally, especially in contested situations, consistent with market practice in the United States. Historically, this has been less so at Luxembourg companies with an EU listing.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

Private settlements with activists are not common in Luxembourg but do occur from time to time.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

Organised shareholder engagement outside of general meetings and earnings calls – through investor days, road shows, presentations at conferences or bilateral contacts – has increased in recent years but tends to vary considerably from company to company. Larger issuers, in particular, tend to organise structural shareholder engagement. Engagement efforts tend to be elevated when the company is faced with a crisis or shareholder discontent (eg, an unsolicited approach or activist campaign, a negative recommendation from proxy advisory firms or poor voting results on say on pay or discharge of directors).

23 Are directors commonly involved in shareholder engagement efforts?

Depending on the company and the topic and shareholder concerned, shareholder engagement efforts may be led by a company's investor relations department or one or more managing or executive directors, – in particular, the CEO or CFO. Non-executive or supervisory directors are less frequently involved in shareholder engagement, though non-executive or supervisory director(s) may lead conversations with investors regarding the performance or remuneration of managing or executive directors.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Certain listed Luxembourg companies have published a policy on bilateral contacts. Companies are not required to disclose shareholder engagement efforts. It is recommended that presentations to institutional or other investors and press conferences be announced in advance, that all shareholders are allowed to follow these meetings and presentations in real time and that the presentations be posted on the company's website after the meeting.

Selective disclosures by a Luxembourg company whose shares are listed on a regulated market within the EEA, must comply with the requirements under the Transparency Act. In addition, Luxembourg companies must ensure equal treatment of all shareholders who are in the same position.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

The explanatory notes to the agenda for a general meeting set out the company's position with respect to the agenda items. The meeting materials are posted on the company's website. Other public communications often take the form of press releases. Listed Luxembourg companies may decide to engage proxy solicitation firms or investor relations specialists to actively reach out to shareholders (particularly Luxembourg companies with a US listing do so in line with US market practice).

Notified major shareholdings (more than 5 per cent) can be found in the online registers. The statutory provisions on identification of shareholders will be amended in the course of 2019 to bring them in line with the revised Shareholders Rights Directive.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

If a shareholder so requests, the (management) board must provide the shareholder, free of charge, with an extract of the information in the company's share register concerning the shares registered in the shareholder's name. Luxembourg companies are not required to provide access to or a copy of the full shareholders register.

If an identification as referred to in question 14 has occurred and shareholders holding 5 per cent of the issued share capital have been identified, the company must disseminate to its shareholders (and publish on its website) any information prepared by the requesting shareholders relating to an agenda item for the general meeting. The company may refuse the request if the information:

- is received less than five days prior to the meeting;
- sends, or may send, an incorrect or misleading signal regarding the company; or
- is of such a nature that the company cannot reasonably be required to disseminate it (criticism of the company's policy or affairs is in itself no valid ground for refusal).

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

Luxembourg, along with other member states, will have to implement the Second Shareholders' Rights Directive , by mid 2019, which includes various amendments to the initial Shareholders' Rights Directive. On 4 February 2019, the Luxembourg justice minister introduced a bill (No. 7402) to amend the current Shareholder Act by transposing the Second Shareholders' Rights Directive. The main purpose is to enhance and harmonise the corporate governance of listed companies across the European Union. The new measures will have a particular focus on encouraging a long-termist view among shareholders and increasing transparency.

NautaDutilh

Margaretha Wilkenhuysen
greet.wilkenhuysen@nautadutilh.com

2 rue Jean Bertholet
1233 Luxembourg
Tel: +352 261 22 91
Fax: +352 26 68 43 31
www.nautadutilh.com

Netherlands

Leo Groothuis, Frans Overkleeft, Paul van der Bijl and Stefan Wissing
NautaDutilh

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The primary source of corporate law is Book 2 of the Dutch Civil Code (DCC). Its provisions are applicable to all companies organised under Dutch law, regardless of their listing venue, and are generally enforced through the civil court system or in proceedings before a specialised court (the Enterprise Chamber of the Amsterdam Court of Appeals).

The primary sources of securities laws are the Dutch Financial Supervision Act (DFSA) and directly applicable EU regulations such as the Market Abuse Regulation (MAR) and the Short Selling Regulation. The DFSA-provisions relating to takeovers of listed companies and disclosure obligations for listed companies and major shareholders apply to all Dutch companies whose shares or depositary receipts for shares are listed on a regulated market within the EEA. The MAR and the Short Selling Regulation apply to (Dutch companies whose) shares or other financial instruments are listed on a regulated market within the EEA. The Dutch Authority for the Financial Markets (AFM) is the competent authority for supervising compliance with the DFSA and, to the extent these regulations allocate competence to the competent authority in the Netherlands, the MAR and the Short Selling Regulation.

A breach of certain statutory provisions of the DCC, the DFSA and the MAR qualifies as a criminal offence, though prosecution is rare.

The revised EU Shareholders Rights Directive, which must be implemented in Dutch law by June 2019, sets out rules on – inter alia – say on pay, identification of shareholders, transmission of information and transparency of institutional investors, asset managers and proxy advisers.

The above statutory requirements are supplemented by the Dutch Corporate Governance Code (DCGC), which was revised in December 2016 and contains principles and best practice provisions regulating relations between the board(s) and shareholders. The DCGC applies to listed Dutch companies, even if the shares are only listed on a stock exchange outside the EEA. While the DCGC applies on a comply-or-explain basis, certain principles and best practices may be considered part of the statutory requirement for board(s) and shareholders to act vis-à-vis each other in keeping with the principles of reasonableness and fairness and may as such be binding.

The Dutch Stewardship Code, developed by pension funds, insurers and asset managers participating in Eumedion, applies since 1 January 2019. It sets out guiding principles for institutional investors with a view to constructive engagement with listed companies on strategy, risk, performance and environmental, social and governance (ESG) aspects, transparency regarding voting policies and their implementation and voting in a well-informed manner with a view to long-term value creation.

Proxy advisory firms such as ISS and Glass Lewis have issued proxy voting guidelines that also cover Dutch-listed companies.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Activist campaigns can play out publicly or privately. Private campaigns can have a significant impact on companies as the considerable pressure put on boards may cause them to change the company's strategy to appease the activist and prevent a public campaign.

Several public activist campaigns played out in 2017 and 2018, including Elliott's campaign against AkzoNobel, CIAM's campaign against Ahold Delhaize and a 'vote no' campaign of four pension funds against Mylan. In addition, there were several court cases about the position of shareholders in listed companies, notably Talpa/TMG (2017) and Boskalis/Fugro (2015–2018), which are relevant to the position of activist shareholders.

The results have been mixed in 2017–2018: Elliott and Boskalis lost their court battles. The 'vote no' campaign against reappointment of Mylan's directors failed; only the non-binding advisory say-on-pay vote was rejected. CIAM did not succeed in getting Ahold to seek shareholder approval for the extension of its takeover defence. Qualcomm raised its offer for NXP following a push by Elliott for a higher price, but ultimately called off the deal. After AkzoNobel successfully fended off the unsolicited approach by PPG and prevailed in litigation initiated by Elliott, it entered into a standstill agreement with Elliott and appointed two new supervisory directors supported by Elliott; in the meantime, it had already announced to sell off its specialty chemicals business.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

Due to Dutch and EU company law reforms introducing new or strengthened shareholder rights around the turn of the 21st century, shareholder activism in the Netherlands rose sharply. After 2007, corrective measures to curb shareholder activism were implemented in the DCC (increased threshold for shareholders to put items on the agenda), the DFSA (lower threshold for notification by major shareholders), the Dutch Corporate Governance Code (response time), case law (strategy falls within the domain of the board) and by listed companies themselves (renewed appreciation for takeover defences available under Dutch law). See also 'Update and trends'.

In the Netherlands, no particular industries are more or less prone to shareholder activism. Activist campaigns against 'national champions' tend to face more backlash from the general public and politicians.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

Historically, activist campaigns have predominantly originated from well-known international activist funds with a global or European investment focus such as Centaurus, Elliott, Hermes, JANA Partners, Knight Vinke, Paulson and TCI. In recent years, fuelled by calls from politicians to take a more active role, Dutch pension funds and other long-term institutional investors have become more vocal.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

High-profile activist campaigns at Dutch companies by activist hedge funds typically focused on a company sale or break-up, increased offer price ('bumpitrage') or return of capital. Long-term institutional investors tend to focus more on ESG topics and executive compensation or 'say-on-pay'.

Factors that tend to attract activists' attention include announced or potential M&A events, low leverage or strong cash positions, as well as perceived corporate governance issues, underperformance and inflated executive pay.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

Depending on the type of activist, its goals and the company's takeover defences, activists may use a number of different tactics to pursue their objectives, such as:

- privately engaging through informal discussions or 'dear board' letters (the starting point of most activist campaigns and the preferred tool of most institutional investors);
- publicly criticising a company's strategy, governance or performance or calling for a sale, break-up, return of capital or bumpitrage;
- short-selling stock and starting a public campaign to drive down stock prices;
- stakebuilding to build up pressure on the boards and signal seriousness;
- partnering with a hostile bidder;
- participating in and voting at general meetings;
- orchestrating a 'vote no' campaign;
- making a shareholders' proposal or requesting an EGM be convened (see questions 7 to 9); or
- initiating litigation (see question 10).

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

Items that shareholders representing individually or collectively at least 3 per cent of a Dutch company's capital request must be included in the convening notice or announced by the company in the same manner, if the company has received the substantiated request or a draft resolution no later than on the 60th day before the day of the general meeting. The company's articles may provide for a lower minimum percentage (eg, 1 per cent, the former statutory threshold) or a shorter period.

The company may refuse to put an item on the agenda as a voting item (rather than a discussion item) if it concerns a matter that falls outside the power of the general meeting. Exceptionally, a company may refuse to put an item on the agenda if it contravenes the principles of reasonableness and fairness.

The Dutch Corporate Governance Code provides that a shareholder should only exercise its right to put items on the agenda after consultation with the (management) board. See question 19 for the (management) board's right to invoke a 180-day response time.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Some listed Dutch companies are subject to the large company regime, in which case the following applies by default. The members of the management board are appointed by the supervisory board (instead of the general meeting) and members of the supervisory board are appointed by the general meeting upon a nomination by the supervisory board. If the binding nomination is not overruled by the general meeting, the person is appointed; if the binding nomination is overruled, the supervisory board shall make a new binding nomination.

The articles of association of many listed Dutch companies that are not subject to the large company regime, provide that the general meeting can only appoint directors upon a binding nomination by the (supervisory) board or that the (supervisory) board may elect to make a binding nomination. The binding nomination can typically be overruled either by absolute majority of the votes cast representing at least one-third of the issued share capital (maximum under the Dutch Corporate Governance Code) or by two-thirds of the votes cast representing more than half of the issued share capital (statutory maximum).

If the appointment of a director is not subject to a binding nomination, a nomination by shareholders can be made in accordance with the procedure set out in question 7 or question 9.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Shareholders representing individually or collectively at least 10 per cent of a Dutch company's capital (or a lower percentage as prescribed in the company's articles) may request the board(s) to convene a general meeting. The request must set out in detail the matters to be discussed. If the board(s) have not taken the steps necessary to hold a general meeting within eight weeks (or six weeks, if the company's shares are not listed on a regulated market within the EEA) after such request, the requesting shareholder may be authorised by the district court in preliminary relief proceedings to convene a general meeting provided that they have a reasonable interest in holding such meeting. As part of the reasonable interest test, the court will weigh the interests of the requesting shareholders against the interests of the company.

See question 19 for the (management) board's right to invoke a 180-day response time.

While shareholders of a Dutch public company may pass resolutions outside a meeting if the company's articles of association so allow, such written resolutions can only be passed by a unanimous vote of all shareholders with voting rights.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Shareholder litigation regarding listed Dutch companies mostly takes place in inquiry proceedings before the Enterprise Chamber. Inquiry proceedings allow shareholders (above a statutory share ownership threshold) of a Dutch company to request the Enterprise Chamber to appoint experts to conduct an investigation into the policy and affairs of the company and to impose certain measures of a definitive or preliminary nature. Depending on the capital structure of the company (ie, low nominal value of the shares), the threshold for an activist to have standing in inquiry proceedings can be very high. The Enterprise Chamber may order an inquiry if the applicant demonstrates that there are well-founded reasons to doubt the soundness and propriety of the company's policy and affairs (eg, deadlock situations; unacceptable conflicts of interest; disturbed relationships; unjustified use of takeover defences). Based on the reported findings of the court-appointed investigators, the applicant may file a petition for a declaratory judgment that mismanagement occurred. At any point during the inquiry proceedings, the Enterprise Chamber may be requested to impose (far-reaching) interim measures by way of injunctive relief (eg, enjoining the execution of board resolutions, appointing one or more independent directors to the board, suspending voting rights of a shareholder or delaying a shareholder vote).

In addition to inquiry proceedings, shareholders can seek nullification of corporate resolutions (arguing for instance that the resolution is contrary to the principles of reasonableness and fairness to be observed) or bring wrongful act claims against a company or its directors (arguing that a particular conduct of the company or its directors constituted a tort against the claimant).

Derivative actions do not exist under Dutch law. The DCC does provide for a collective action, initiated by a foundation or association whose objective is to protect the rights of a group of persons having similar interests. Presently, such action cannot result in an order for payment of monetary damages but may only result in a declaratory judgment. To obtain compensation for damages, individual claimants may file follow-on suits based on the declaratory judgment. Alternatively, in order to obtain compensation for damages, the foundation or association and the defendant may reach a settlement, which can subsequently be declared binding upon all injured parties by the Amsterdam Court of Appeal with an opt-out choice for an individual injured party. A bill is currently pending before the Dutch Senate that would remove the restrictions on seeking monetary damages on a collective basis while at the same time imposing additional requirements on collective action organisations as well as enhanced admissibility thresholds for collective actions.

At general meetings of Dutch companies, boards are required to provide the shareholders with all the information requested by them, unless doing so would be contrary to an overriding interest of the company. While the concept of discovery does not exist under Dutch law, a party with a legitimate interest may submit a motion to the court demanding the production of specified documents pertaining to a legal relationship to which the requesting party or its legal predecessor is a party.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

Under Dutch law, shareholders may - in principle - give priority to their own interests. However, they must act vis-à-vis each other and the board(s) in keeping with the principles of reasonableness and fairness. Courts apply an 'all facts and circumstances' test to determine whether an act was in keeping with such principles. The Dutch Corporate Governance Code adds that this includes a willingness to engage with the company and fellow shareholders, and that the greater the interest of the shareholder in a company, the greater is his or her responsibility to the company, fellow shareholders and other stakeholders.

Compensation

12 May directors accept compensation from shareholders who appoint them?

There is no Dutch law that prohibits a director of a Dutch company from accepting compensation from a shareholder who nominated or appointed him or her. Irrespective of whether a director is nominated, appointed or compensated by a specific shareholder, Dutch corporate law requires all directors to be guided by the corporate interests of the company and its business in performing their duties and to consider with due care the interests of all stakeholders. To the extent that any such compensation creates, in respect of a particular board matter, a direct or indirect personal interest for the director that conflicts with the interests of the company and its business, the director may not participate in the deliberations and decision-making of the board on that matter.

The Dutch Corporate Governance Code considers a director non-independent if it is a representative of a 10 per cent-shareholder. Being a shareholder representative generally involves receiving compensation from such shareholder. Therefore, compensation received by a director from a 10 per cent-shareholder is indicative of being a shareholder representative and is a relevant factor in determining that director's independence.

Mandatory bids

13 Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

The Dutch mandatory offer rules only apply to Dutch public companies whose shares or depositary receipts for shares are listed on a regulated market within the EEA. Pursuant to the DFSA and subject to limited exemptions, a mandatory offer requirement is triggered if a person, or a group of persons acting in concert, obtains the ability to exercise at least 30 per cent of all outstanding voting rights in a company (predominant control).

Concert parties are natural persons, entities or companies collaborating under an agreement with the purpose to acquire predominant control in a company or, if the target company is one of the collaborators, to thwart an announced public offer for such target. Persons, entities and companies are in any event deemed to act in concert with: (i) entities that are part of the same group; and (ii) their subsidiaries or other controlled entities. Enforcement of the obligation to make a mandatory bid rests with the Enterprise Chamber, which – as an independent judicial authority – is not bound by ESMA's white list on acting in concert.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Pursuant to the DFSA, any person who acquires or disposes of shares or voting rights of a Dutch company whose shares are listed on a regulated market within the EEA, must forthwith (generally, the next trading day) notify the AFM if the percentage of capital interest or voting rights reaches, exceeds or falls below any of the following thresholds: 3, 5, 10, 15, 20, 25, 30, 40, 50, 60, 75 and 95 per cent. Notifications are published in the AFM's online registers. The DFSA does not require shareholders to disclose their intentions.

At a few listed Dutch companies, the articles of association impose additional notification obligations on shareholders.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

Depositary receipts for shares, convertible bonds, options for acquiring shares, cash settled instruments of which the value is at least in part dependent on the value of shares (eg, contracts for difference and total return swaps) and any other contracts creating a similar economic position are taken into account for purposes of calculating the percentage of capital interest and voting rights.

For purposes of calculating the percentage of capital interest and voting rights held by a person, shares and voting rights held by such person's controlled entity, by a third party for such person's account or by a third party with whom such person has concluded an agreement to pursue a sustained joint voting policy, are taken into account.

Any person who acquires or disposes of financial instruments as a result of which such person's gross short position reaches, exceeds or falls below the thresholds mentioned in question 14, must forthwith notify the AFM. Notifications are published in the AFM's online registers. In addition, the EU Short Selling Regulation requires any person holding a net short position to privately notify the relevant competent authority the next trading day if the position reaches or falls below 0.2 per cent (and each 0.1 per cent above that) of the issued share capital of a Dutch listed company. Notifications for a net short position of 0.5 per cent or above are made public.

Insider trading

16 | Do insider trading rules apply to activist activity?

Yes, the MAR applies with respect to Dutch companies whose shares or other financial instruments are listed on a regulated market within the EEA. Pursuant to the MAR, no person may:

- engage or attempt to engage in insider dealing;
- recommend that another person engage, or induce another person to engage, in insider dealing;
- unlawfully disclose inside information; or
- engage, or attempt to engage, in market manipulation.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

Dutch corporate law requires all directors to be guided by the corporate interests of the company and its business in performing their duties. If the company has a business, the interests of the company generally are particularly defined by the interest of promoting the sustainable success of the company's business (ie, a focus on long-term value creation, as also expressed in the Dutch Corporate Governance Code). Under Dutch law, there is no duty to maximise shareholder value at all costs. Instead, boards must weigh all relevant aspects and circumstances and shall consider with due care the interests of all stakeholders, including shareholders, employees, creditors and business partners. Boards have a large discretion on how to weigh the various stakeholders' interests against each other, although the duty of care may require boards to prevent unnecessary or disproportionate harm to the interests of specific stakeholders. The (management) board is responsible for determining and implementing the strategy of the company (in a two-tier board structure: under supervision of a supervisory board).

Responding to an unsolicited approach or activist proposal seeking to change the company's strategy (including by means of efforts to change the board composition) forms part of the company's strategy and, as such, falls within the domain of the board. There is no shift of fiduciary duties: the directors must continue to act in the best interests of the company and its business with a view to long-term value creation, taking into account the interests of all stakeholders. Boards should ensure that they have all relevant information to make an informed decision and the proposal should be carefully reviewed, without bias, and assessed against all available alternatives. Shareholders do not have to be consulted prior to the company's response; boards are (retrospectively) accountable to the shareholders.

Dutch case law confirms the absence of a general obligation for boards to engage with a bidder or activist to discuss the proposal. While boards may 'just say no', they should do so only after careful consideration of a serious proposal on its merits and boards should consider whether some form of interaction with the bidder or activist is needed to make sure the directors have all relevant information to make an informed decision.

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

Although the absolute number of activist campaigns in the Netherlands is limited, the uptick in (high-profile) activist campaigns in recent years has made shareholder activism and engagement a discussion topic in the boardroom of many listed Dutch companies. No company is immune to activism and preparedness is key. While recommended advance preparations depend on the specifics of the company, a few useful preparations are:

- continuously monitoring market activity, financial performance (particularly relative to peers) and the company's industry and competitors;
- setting up a small defence team of key directors or officers plus legal counsel, investment banker and public relations firm that meets periodically;
- 'thinking like an activist', routinely assessing the company's strengths and weaknesses and its takeover defences and exploring available strategic alternatives (consider red teaming);
- building relationships and credibility with shareholders and other stakeholders before activists emerge and maintaining regular contact with major shareholders, the marketplace generally and key stakeholders; and
- communicating clearly and consistently on ESG and corporate social responsibility matters, the company's long-term strategy, its implementation and the progress in achieving it.

Defences

19 What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Most listed Dutch companies have adopted one or more structural take-over defences, often in their articles of association. Examples include:

- binding nomination rights and supermajority requirements for appointment and involuntary dismissals of directors;
- staggered boards;
- evergreen call option for preference shares to an independent Dutch foundation whose purpose is to safeguard the interests of the company and its stakeholders and resist any influences that might adversely affect or threaten the company's strategy, independence or continuity in a manner contrary to such interests, pursuant to which the foundation can effectively acquire up to 50 per cent of the votes;
- loyalty voting shares, providing for additional voting rights for 'loyal' shareholders;
- priority shares with certain control rights; or
- listing of depositary receipts for shares rather than the shares itself.

In addition, Dutch companies may use a variety of other tactics such as:

- engaging with the activist, which may result in some form of agreement (see question 21);
- engaging with shareholders and other stakeholders (eg, convince major shareholders with compelling long-term plans or mobilise employees, customers or politicians);
- invoking a response time under the Dutch Corporate Governance Code, pursuant to which the (management) board may stipulate a reasonable period of up to 180 days if shareholders seek to convene an EGM or put items on the agenda that may result in a change in the company's strategy (eg, dismissal of directors) and during which the board should deliberate, consult stakeholders and explore alternatives (according to case law, such response time must be respected by shareholders absent an overriding interest);
- invoking the put-up-or-shut-up rule under the Dutch public offer rules;
- exploring strategic transactions that make the company a less desirable target;
- issuing new shares (under existing authorisations) or selling treasury shares to a friendly third party (white knight); or
- issuing bonds with a mandatory redemption at a higher value in case of a change of control (macaroni defence).

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

It depends on the listing venue. Dutch companies with a US listing often (choose to) receive regular updates on the vote tally, especially in contested situations, consistent with market practice in the United States. Historically, this has been less so at Dutch companies with an EU listing. In recent years, the practice in the Netherlands has shifted more towards the US practice of companies receiving updates on the vote tally prior to the general meeting.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

While private settlements with activists are not common in the Netherlands, they do occur from time to time. A company may seek to enter into a pure standstill agreement to reach a truce with an activist shareholder in return for, for instance, a commitment to consult the activist (and other major shareholders) on new director nominations. In case of activists with a significant shareholding, a settlement may take the form of a relationship agreement wherein the company and the shareholder agree on topics such as strategy and governance and wherein the company may give one or more (supervisory) board seats to the activist.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

Organised shareholder engagement outside of general meetings and earnings calls, through investor days, road shows, presentations at conferences or bilateral contacts, has increased in recent years but tends to vary considerably from company to company. Especially larger issuers tend to organise structural shareholder engagement. Engagement efforts tend to be elevated when the company is faced with a crisis or shareholder discontent (eg, an unsolicited approach or activist campaign, a negative recommendation from proxy advisory firms or poor voting results on say-on-pay or discharge of directors).

In line with the recommendation of the Dutch Corporate Governance Code, most listed Dutch companies have formulated an outline policy on bilateral contacts with shareholders and posted such policy on their website. Mostly, such policies leave large discretion to the company to decide whether to enter into, continue or terminate any dialogue and to determine the company participants for such meetings.

23 Are directors commonly involved in shareholder engagement efforts?

Depending on the company and the topic and shareholder concerned, shareholder engagement efforts may be led by a company's investor relations department or one or more managing or executive directors, in particular, the CEO or CFO. Non-executive or supervisory directors are less frequently involved in shareholder engagement, though non-executive or supervisory directors may lead conversations with investors regarding the performance or remuneration of managing or executive directors.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Most listed Dutch companies have published a policy on bilateral contacts (see question 22). Companies are not required to disclose shareholder engagement efforts. The Dutch Corporate Governance Code does recommend that presentations to institutional or other investors and press conferences be announced in advance, that all shareholders be allowed

to follow these meetings and presentations in real time and that the presentations be posted on the company's website after the meeting.

Selective disclosures by a Dutch company whose shares are listed on a regulated market within the EEA, must comply with the requirements under the MAR. In addition, Dutch companies must ensure equal treatment of all shareholders who are in the same position.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

See question 24 for rules on selective or unequal disclosure.

The explanatory notes to the agenda for a general meeting set out the company's position with respect to the agenda items. The meeting materials are posted on the company's website. Other public communications often take the form of press releases. Listed Dutch companies may decide to engage proxy solicitation firms or investor relations specialists to actively reach out to shareholders (particularly Dutch companies with a US listing do so in line with US market practice).

Notified major shareholdings (greater than 3 per cent) can be found in the online AFM registers. In addition, a listed Dutch company whose shares trade in book-entry form through Euroclear Nederland can – at its own initiative or upon a timely request by shareholders representing at least 10 per cent of the company's capital – run a process in the lead-up to a general meeting to identify its shareholders holding 0.5 per cent or more of the company's capital. The company may approach Euroclear Nederland and relevant intermediaries to provide certain information on the identity of the company's shareholders. The company must keep such information confidential. The company may use such information to disseminate information to its shareholders, provided it also posts such information on its website. The statutory provisions on identification of shareholders will be amended in the course of 2019 to bring them in line with the revised Shareholders Rights Directive.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

If a shareholder so requests, the (management) board must provide the shareholder, free of charge, with an extract of the information in the company's share register concerning the shares registered in the shareholder's name. Dutch companies are not required to provide access to or a copy of the full shareholders register. See also question 10 regarding rights of shareholders to information.

If an identification as referred to in question 25 has occurred and shareholders holding 1 per cent of the issued share capital or shares with a value of at least €250,000 so request, the company must disseminate to its shareholders (and publish on its website) any information prepared by the requesting shareholders relating to an agenda item for the general meeting. The company may refuse the request if the information:

- is received less than seven business days prior to the meeting;
- sends, or may send, an incorrect or misleading signal regarding the company; or
- is of such a nature that the company cannot reasonably be required to disseminate it (criticism of the company's policy or affairs is in itself no valid ground for refusal).

NautaDutilh

Leo Groothuis
leo.groothuis@nautadutilh.com

Frans Overkleeft
frans.overkleeft@nautadutilh.com

Paul van der Bijl
paul.vanderbijl@nautadutilh.com

Stefan Wissing
stefan.wissing@nautadutilh.com

Beethovenstraat 400
1082 PR Amsterdam
Netherlands
Tel: +31 20 71 71 000
Fax: +31 20 71 71 111
www.nautadutilh.com

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

In recent years, high-profile unsolicited approaches and increasing pressure from activists have prompted a public debate in the Netherlands on the dangers of short-termism and the effectiveness of defence measures available to listed Dutch companies.

In December 2018, the Dutch government published draft legislation that, if enacted in its current form, introduces a statutory cooling-off period of up to 250 days that the board may invoke in case of an unsolicited takeover bid or when faced with activists proposing to dismiss, suspend or appoint board members, if such bid or proposal materially conflicts with the interests of the company and its business (as reasonably determined by the board). During the cooling-off period, the general meeting cannot validly resolve on the dismissal, suspension or appointment of board members, unless proposed by the board itself.

Shareholders representing 3 per cent or more of the company's capital may request the Enterprise Chamber for early termination of the cooling-off period. The Enterprise Chamber must deny the request if the board, in view of the circumstances at hand when the cooling-off period was invoked, could reasonably have come to the conclusion that the bid or proposal constituted a material conflict with the interests of the company and its business. The cooling-off period also ends early if the hostile bid is declared unconditional.

The cooling-off period is aimed at taking some of the (short-term) pressure off of target boards, to allow for a careful decision-making process in which – in accordance with the Dutch stakeholder model – the interests of all stakeholders are considered and weighed with a view to long-term value creation.

The legislation would apply to all Dutch companies whose shares or depositary receipts for shares are listed on a regulated market or MTF in the EEA or any similar stock exchange outside the EEA (eg, Nasdaq and NYSE).

New Zealand

David Raudkivi
Russell McVeagh

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The vast majority of entities in New Zealand that may be subject to shareholder activism and engagement are companies established under the Companies Act 1993. Companies that are listed on the New Zealand Stock Exchange (known as NZX) are subject to the NZX Listing Rules. The Takeovers Code also applies to all companies listed on the NZX and to companies that have a broad shareholding (see below).

The other principal legislation is the Financial Markets Conduct Act 2013 and the Financial Markets Conduct Regulations 2014, which regulate misleading and deceptive conduct in relation to dealings in securities, enforce a substantial product disclosure regime and impose restrictions on the making of unsolicited offers to acquire securities.

The Companies Act and the Financial Markets Conduct Act were passed by parliament and the regulations under each of these are made and amended by the Governor-General on the recommendation of the Minister of Commerce and Consumer Affairs, granted under the authority of the relevant primary legislation.

The NZX Listing Rules are made and enforced by NZX Limited, as operator of the New Zealand Stock Exchange, with oversight from the Financial Markets Authority.

The Companies Act and the constitution of each relevant company are of principal relevance for any activism and shareholder engagement as they provide for the rights and requirements of shareholders in convening a shareholder meeting, the right to propose resolutions and explanatory statements and form the basis for the substantial body of corporate governance law.

The Takeovers Code is a regulation made by Order in Council on the recommendation of the Minister of Commerce and Consumer Affairs under the Takeovers Act 1993, and prescribes a code for the conduct of takeovers of 'code companies'. A code company includes any company incorporated in New Zealand and listed on the NZX; or which has 50 or more shareholders and 50 or more share parcels, even if not listed. The Takeovers Code is enforced by the Takeovers Panel.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Like most jurisdictions, the prevalence of observable shareholder activism in New Zealand has grown during the past few years.

Most shareholder activism occurs on a private basis, at least initially, and only a percentage develop into a public campaign where there is a noticeable outcome. It is therefore difficult to establish specific data or statistics. The nature of the types of activist engagement traverses the typical spectrum seen in most other jurisdictions, ranging from de facto/proxy takeovers and director-election contests, to 'vote no' campaigns and advocacy in relation to board and management remuneration.

For the most part, company boards take activist engagement very seriously and respond to activists in good faith to understand their concerns. This can result in alignment and adoption of some or all of the strategic changes to the company that have been proposed by the activist or a change in the board of directors without any public activist presence. Alternatively, where activism develops into a public campaign, results can vary with corporate changes agreed or board resignations after the publicity develops but before a vote ever takes place. Very few campaigns go to a vote and, for those that do, the results can be close.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

Generally regulators do not take a position on activism. The relevant regulators, particularly the Financial Markets Authority and the Takeovers Panel, frequently receive complaints from stakeholders during a campaign and generally do not get involved unless it is clear that the conduct in question breaches specific provisions of the Takeovers Code or relevant legislation. Shareholders have been censured for timely failure to disclose substantial product holder positions or for misleading conduct.

Shareholder activists in New Zealand are not restricted to any particular industry. However, there is a strong concentration of listed companies on the NZX that have controlling shareholders through being majority owned by the New Zealand Government (for example, three of the major energy companies and Air New Zealand) or having a strategic controlling shareholder. Naturally, these companies are less prone to activism.

Like other jurisdictions, targets are typically identified by poor operational or share price performance, high cash balances, untapped or mismanaged opportunities, governance issues, and perceived consolidation or buy-out opportunities.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

Significant activists tend to be long-term shareholders, including institutional investors and KiwiSaver (superannuation) funds. However, due to the relative ease of proposing shareholder resolutions, activists can also include disgruntled minority shareholders. Occasionally, industry participants also engage in activism on a strategic basis, but this is generally not as successful or as well received as a takeover

transaction. Shareholding percentages need not be particularly significant to have an impact.

Institutional shareholding in New Zealand has become more concentrated in recent years due to the continued growth of New Zealand superannuation contributions to KiwiSaver funds. However, for the most part, these tend to be passive investors and are more likely to abstain than be seen to support an activist in any proxy campaign. However, this naturally enhances the votes held by the activists when only the shares that vote are taken into account. Unlike some jurisdictions, there is no requirement for KiwiSaver funds, among others, to periodically disclose how they have voted.

While we see alliances form between shareholders where there is mutual support in a campaign, it is not uncommon to see these fall apart through a sale of shares by a party during the course of the campaign or a shareholder reaching a satisfactory accommodation with the target on their issues.

Investors who consider engaging in an activist strategy are also likely to be mindful of any possible effect on their reputations and how activism could affect their further participation in IPOs or other corporate opportunities.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

The main areas on which shareholder activism focuses are:

- Change-of-board campaigns or director-appointment campaigns.
- Vote-no campaigns to shareholder resolutions.
- Shareholder and hedge fund activism in connection with a value strategy manifested through a shareholder proposal. These can range from players looking to elevate the share price quickly for profit, or those looking to effect a genuine long-term value-added strategy for the company.
- Say on pay. There are no express provisions for shareholder say on management pay in New Zealand. However, director pay is a direct focus for the New Zealand Shareholders' Association, which regularly takes published positions on director remuneration resolutions and votes discretionary proxies from its members. In particular, the Shareholders' Association generally takes the position that the requested director fee increase must be demonstrated to be reasonable and, where remuneration benchmarking reports are used to justify fee increases, the full report should be made available to shareholders. Fee pools, and the fees paid to directors, should be comparable with the company's peers and the peer group companies should be of a similar scale and the directors should take into account the overall performance of the company prior to asking shareholders to approve a fee increase. In this regard, it may be more appropriate to reduce the number of directors rather than seek an increase. In this context, it has been apparent that smaller, more regular, increases are more likely to be palatable than a single large increase.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

Generally, activist strategies begin with private discussions directly with the subject company to negotiate changes in line with the activist's value strategy. These may then develop into public campaigns, media campaigns and greater pressure from a broader shareholder base.

Shareholder resolutions and proxy contests are generally a last resort.

There is no set playbook and examples differ depending on the company's specific situation, its shareholder agendas and share register.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

Clause 9(1) of the First Schedule of the Companies Act provides that any shareholder can put up a resolution at a shareholders' meeting by giving written notice to the board, notifying the proposal or text of the proposed resolution.

Provided that the shareholder offers the notice well in advance, the company is required to bear the subsequent cost of including the information in the notice of meeting. The shareholder is also permitted to include an explanatory statement of not more than 1,000 words on the resolution, together with his or her name and address.

There are limited rules that operate to exclude only a few types of resolutions. The board may only refuse to include a shareholder-proposed resolution in the notice of meeting if the directors consider the resolution to be defamatory (within the meaning of the Defamation Act 1992). The board may only refuse to include an accompanying statement if it is defamatory, frivolous or vexatious.

Instead, the rules focus mainly on timing and who bears the cost of putting the proposal. Specifically, where the notice is received at least 20 working days before the last day for giving notice of the meeting, the board must give notice of the proposal and text of the resolution at the company's expense. If the notice is received between five and 20 days before the last date, the shareholder is required to bear the cost. If the notice is received less than five days before the last date, putting that proposal to shareholders is at the board's discretion.

Shareholder resolutions can have the effect of appointing and removing directors or changing the constitution. Section 109(2) of the Companies Act provides that notwithstanding anything in the Act or constitution, a meeting of shareholders may pass a resolution relating to the management of a company. However, section 109(3) goes on to provide that unless the constitution provides that the resolution is binding, it is not binding on the board. Therefore, an ordinary resolution that relates to the future direction of the company will generally be advisory only. It would nonetheless be a brave board that ignores such a steer from shareholders when the same voting thresholds would ordinarily apply to effect a change in the directors who sit on the subject board.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

The NZX Listing Rules specifically require the board of the company to call for nominations from shareholders and impose director rotation requirements. To properly inform shareholders, the company will invariably include any requested biography and other reasonable explanatory statement provided by the candidate for election, at the company's cost.

The procedures referred to in relation to question 7 also naturally apply to shareholder-proposed resolutions for the election of directors.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Under section 121 of the Companies Act, a shareholder or group of shareholders commanding at least five per cent of the company's voting

rights have the ability to require the board to call a special meeting of shareholders. While the board or the court can only convene a meeting if it is in the interests of the company, shareholders are not limited in this way and are free to do so if this simple percentage threshold requirement is met.

Neither the Companies Act nor the NZX Listing Rules specify any specific timeframe within which the board is required to convene a meeting upon receiving valid notice from shareholders.

Case law has also been limited on the duties of the board to convene a meeting. However, proceedings requiring the board to convene a meeting under section 121(b) of the Companies Act can be brought seeking injunctive relief, which requires the courts to take into account the balance of convenience and the overall justice of the matter. Accordingly, courts commonly accept the principle that a meeting must be called within a 'reasonable time'. What is reasonable must be assessed against the particular circumstances presented before the court.

Under section 109 of the Companies Act, the chairperson at a meeting of shareholders must allow a reasonable opportunity for shareholders to question, discuss or comment on the management of the company as part of the general business at a meeting.

Shareholders may also act by written resolution. However, this is extremely rare in a public company context. Generally, a resolution in writing signed by not less than 75 per cent of the shareholders entitled to vote on that resolution who together hold not less than 75 per cent of the votes is as valid as if it had been passed at a meeting of those shareholders.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

The Companies Act provides a number of statutory remedies for minority (and, in some cases, majority) shareholders. These include rights to:

- apply for relief on the ground that the company's affairs or acts are 'oppressive, unfairly discriminatory, or unfairly prejudicial';
- apply for the company's liquidation on the ground that 'it is just and equitable' to do so;
- apply for an injunction restraining the company or a director from breaching the constitution or provisions of the Act;
- apply for a compliance order requiring a director or the company to take any steps required to comply with the constitution or the Act;
- bring an action against a director or the company for breach of a duty owed to the shareholder personally; or
- bring a statutory derivative action with the leave of the Court.

While derivative actions are not particularly common, section 165 of the Companies Act gives the court the ability to grant leave to a shareholder or director of a company to bring proceedings in the name and on behalf of the company or intervene in proceedings to which the company is a party for the purpose of continuing, defending, or discontinuing proceedings on behalf of the company. In essence, the section facilitates the enforcement of directors' duties owed to the company where the company has failed to take the necessary enforcement steps.

While the section does not expressly limit the remedy to minority shareholders, the prevailing view is that a shareholder with a controlling interest should not generally be permitted to use the derivative procedure. There are a number of requirements the court must consider before granting leave to allow derivative actions, including:

- Being satisfied that the company does not intend to bring, diligently continue or defend, or discontinue the proceedings. In this regard, the party proposing to bring derivative proceedings must inform the court as to the extent of their effort to convince the company to take action against the directors.
- Being satisfied that it is in the interests of the company that the conduct of the proceedings should not be left to the directors or to the determination of the shareholders as a whole. This may be appropriate in instances of deadlock, cessation of trading and wrongdoer control, where the court considers that it would be in the best interests of the company to sidestep its internal processes for making decisions.

The court must also consider the following four mandatory factors under section 165(2):

- the likelihood of the proceedings succeeding;
- the costs of the proceedings in relation to the relief likely to be obtained;
- any action already taken by the company or related company to obtain relief; and
- the interests of the company in the proceedings being commenced, continued, defended, or discontinued.

Under section 178 of the Act, a shareholder may request that a company disclose 'information' held by the company to the shareholder. The company must either provide the information or refuse to provide the information and specify the reasons for the refusal. A company is entitled to a reasonable time period to provide the information and may impose a reasonable charge for the service. Without limiting the reasons for which a company may refuse to provide information, a company may refuse to provide information if:

- the disclosure of the information would, or would be likely to, prejudice the commercial position of the company;
- the disclosure of the information would, or would be likely to, prejudice the commercial position of any other person, whether or not that person supplied the information to the company; or
- the request for the information is frivolous or vexatious.

A shareholder who is dissatisfied with a refusal by a company to supply information may appeal that decision to the court. The courts have held that a request for information, when it is possible that such information may be used as part of a due diligence exercise for a takeover offer, may be declined.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

Shareholders do not generally owe any fiduciary duties to the company, regardless of the size of their shareholding. Directors who represent a shareholder activist on the board of the target company owe the same duty to act in good faith and in the best interests of the company as all other directors.

Compensation

12 May directors accept compensation from shareholders who appoint them?

Board members of listed companies are typically remunerated by the relevant company in accordance with an overall level of compensation that has been approved by the company's shareholders under the NZX

Listing Rules. Any increase in the number of directors typically results in an automatic corresponding increase in the fee pool to allow equivalent compensation to be paid to the additional director.

However, a director nominee of a shareholder may be separately remunerated by the shareholder under the terms of his or her employment contract or terms of appointment but the director should ensure that they make appropriate disclosure of their interests in the company's interests register as required under the Companies Act.

Mandatory bids

13 | Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

Under the Takeovers Code, the acquisition by a person (together with that person's associates) of more than 20 per cent of the voting rights in a listed company must be undertaken in accordance with the Code (ie, pursuant to a takeover offer in accordance with the prescribed process set out in the Code or with the approval of an ordinary resolution of the target company's shareholders).

The process for a takeover offer requires a notice of intention to make an offer. The offeror may then send a takeover offer during the period 14 to 30 days after their notice of intention to make the offer has been given. However, there is no 'put up or shut up' rule, so the offeror may let its offer lapse and follow up with a further notice of intention to make a takeover offer without being subject to any stand-down period.

The Takeovers Code applies to aggregate holdings of 'associates' (as that term is defined in the Code) but there are generally no restrictions on shareholders agreeing to act in concert provided that neither shareholder acting in association acquires shares while their combined shareholdings exceed the 20 per cent threshold and the shareholders comply with the substantial product holder disclosure regime (see question 14) to disclose their relevant interest.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Yes. Part 5 of the Financial Markets Conduct Act requires persons who have a 'relevant interest' in 5 per cent or more of a class of quoted voting securities of a listed issuer to make immediate disclosure by means of filing a 'substantial product holder notice' with the NZX and the relevant issuer.

A person must disclose that interest in the prescribed form as soon as the person knows, or ought reasonably to know, that they have become a substantial product holder.

There is then a requirement to disclose any change in the nature of the substantial holding, any movement of 1 per cent or more in the relevant interest held, and upon ceasing to be a substantial product holder.

The rules do not require the holder of the relevant interest to disclose their intentions.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

The Financial Markets Conduct Act specifically provides that if a person has a relevant interest in a derivative over quoted voting security, they are treated as having a relevant interest in the underlying voting security, which must be disclosed if the thresholds or circumstances referred to in question 14 are met.

The Act specifically also defines a 'relevant interest' to capture interests held by another person if (among other things) the other person or its directors are accustomed or under an obligation (whether legally enforceable or not) to act in accordance with the first person's directions, instructions, or wishes in relation to the voting security, the first person controls 20 per cent or more of the other person, or they have an agreement to act in concert in relation to the voting security.

A short position itself may not necessarily need to be disclosed but the fact of any borrowing of quoted voting securities or subsequent disposal of those securities may need to be disclosed if any interest at a point in time exceeds 5 per cent of the voting securities on issue.

Insider trading

16 | Do insider trading rules apply to activist activity?

The Financial Markets Conduct Act includes specific insider trading restrictions. An 'information insider' is prohibited from trading quoted financial products of a listed issuer. An 'information insider' is a person who has material information relating to the listed issuer that is not generally available to the market and knows, or ought reasonably to know, that the information is material information that is not generally available to the market.

It is possible that, through engagement and the provision of information, an activist could become an 'information insider' and it would be appropriate for the activist and target company to enter into a confidentiality and standstill agreement if material non-public information is to be disclosed.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

Directors are subject to a general duty to act in good faith and in the best interests of the company. This applies in the same way in relation to responding to an activist proposal. Generally, this leads to constructive engagement with the activist and consideration of the full or partial adoption of any accretive strategies. The board will also need to consider the provision of information carefully, given continuous disclosure obligations.

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

There are no structural defences to shareholder activism that we would typically recommend. Defensive tactics, such as poison pills or rights plans, would generally run afoul of the prohibition on defensive tactics in the Takeovers Code and would likely be inconsistent with the duties of directors to exercise their powers for a proper purpose and in the best interests of the company. Generally, New Zealand's corporate law regime is seen as shareholder friendly and gives a number of rights to shareholders summarised elsewhere in this questionnaire to support the engagement.

Companies should generally have a policy in place that outlines procedures to be followed in relation to an activist approach or a takeover proposal, including consideration of continuous disclosure obligations, contact details for trusted advisers and protocols for engagement – including requirements for a script, and record keeping and confidentiality expectations.

We do not see shareholder activism causing any greater concern in the boardrooms of New Zealand companies than it does in any other jurisdictions.

Defences

19 What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

In addition to good management practices, in order to avoid being the target of shareholder activism, companies should look to maintain a strong investor relations programme. This includes providing regular market updates and clear communication of the company's business strategy. Investors appreciate opportunities to ask questions on conference calls at the time results are announced. Companies also generally benefit from a good understanding of the interests of significant shareholders on the register and their perspectives (if they are willing to share them).

Monitoring movement in the share register is also important. Particular issues can arise where a particular shareholder is overweight in the company's shares and needs to generate exit options.

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

The company's share registrar normally provides proxy updates daily or upon request to a company in advance of a shareholder meeting. They are typically not disclosed other than the chairman stating at the meeting the number of proxies held and how they are directed to be cast on the resolution. Care needs to be taken with this information in advance of the meeting as it could be considered inside information in relevant circumstances – although institutional investors tend to deliver proxies very shortly before the deadline by which proxies must be received (usually 48 hours before the meeting) so the information may only become meaningful and reliable at that point in time.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

Private settlements or accommodations of activist agendas are, we understand, much more common than fully-fledged public campaigns resulting in shareholder meetings and votes. It is reasonably common to see outcomes with changes in one or more board seats, directors not standing for re-election, and companies agreeing a compromise position to adopt one or more of the strategies or outcomes advocated for by the activist.

Other than for changes in the directors and management, such outcomes may or may not be publicly announced – and the target company will need to have careful consideration of its continuous disclosure obligations in this regard.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

Engagement with shareholders is principally undertaken through continuous disclosure, which is a critical focus of NZX as market supervisor. Many listed issuers have also focused on improving their shareholder engagement in recent years through their investor relations functions and endeavours to provide shareholders with a greater understanding of the business at annual meetings and in shareholder communications. It is not unusual for companies to provide shareholders with access to products or facilitate visits. It is also typical for issuers to hold conference calls to facilitate Q&A at the time of announcing annual and half-year results.

23 Are directors commonly involved in shareholder engagement efforts?

Normally the company's senior management lead any response, but depending on the nature of the proposals – for example, if they concern board or management appointments or changes – independent directors, and in some cases the chair, may also become involved in the engagement.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

All listed issuers are subject to a continuous disclosure regime under the NZX Listing Rules, which require the immediate disclosure of any material non-public information unless an exception to disclosure applies. It is generally permissible to hold back information that is confidential and concerns an incomplete proposal or negotiation if the objective standard is met that a reasonable person would not expect disclosure. Accordingly, it is possible for most shareholder engagement efforts to play out in private.

It is only when the matter becomes public, such as through a media campaign or open letter, that the company may be compelled to make disclosure through the market announcement platform.

Most issuers would consider a requisition of a shareholder meeting and the requirement to put a shareholder resolution as a matter that triggers a continuous disclosure obligation and make disclosure to the market.

For these reasons, a company should also require an activist to sign a confidentiality agreement before sharing material information. However, that activist may not want to receive such information so as to avoid becoming an 'information insider' and thereby be restricted from trading in the target company's shares while it is in that position.

There is no prescribed form of disclosure, provided that the information disclosed is sufficient to properly inform the market of all material matters. In the case of a demand to call the meeting, this will often include disclosing the form of requisition itself or the text of the resolution proposed.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

Under the NZX Listing Rules, a company is required to disclose all communications it provides to its shareholders through the market announcement platform. However, this does not apply to investor relations materials, personalised letters or dividend and transfer statements. Such requirements do not apply to communications emanating

from third parties and nor do third parties have the right to post such information on the target company's NZX announcement page. Generally, there are no restrictions on shareholder communications, as long as they are not misleading or deceptive.

Proxy solicitation firms are active in New Zealand and can be seen to operate in relation to some takeovers and other major corporate events for significant companies. In a takeover situation, if the proxy solicitation firm represents an offeror or target company, the Takeovers Panel expects to receive a copy of any script or other communication material, which may also lead to requests from the offeror or target to obtain a copy.

Most shareholders opt to receive electronic communications by email through agreement in writing with the issuer, so it is typical for shareholder engagement to proceed in that manner for shareholders who have agreed to that mode of communication.

Care needs to be taken in relation to proxy solicitation not to become the holder or controller of more than 20 per cent of the voting rights of the target company in breach of the Takeovers Code. In this regard, there is an exemption for proxies appointed after the notice of meeting has been despatched, provided that the proxy does not pay consideration to receive the proxy.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

Significant shareholding positions above 5 per cent in listed issuers are disclosed through the substantial product-holder disclosure regime discussed in question 14, which is easily accessed through NZX's website. A listed issuer is also required to summarise these holdings in its annual reports.

Under the Financial Markets Conduct Act, issuers of securities that have been offered to the public are generally required to keep a securities register, make that register available for public inspection upon notice and provide copies of the register to any person on request and on payment of any prescribed fee. When a copy of the register is requested, the reasons for the request and intended purpose must be disclosed and the issuer may provide a copy of that statement to the Financial Markets Authority. The Financial Markets Authority may determine that the issuer is not required to comply with the request to provide the copy of the register.

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

New Zealand has seen a greater concentration of institutional investors through the increasing investments held by KiwiSaver funds for superannuation contributions. Corporate activity has been focused on takeovers under traditional tender offer structures and by scheme of arrangement, which has seen the number of companies listed on the New Zealand Stock Exchange decrease noticeably.

In this regard, NZX (which is itself a listed company) has experienced activist engagement in the public arena, originating from a fund investor.

The New Zealand Shareholders' Association has also played an important role and regularly now publishes its position on significant corporate transactions and director remuneration resolutions. It is an important stakeholder as it commonly votes as proxy on behalf of its retail shareholder members. The New Zealand Shareholders' Association played a particularly activist role in relation to the re-election of a Rakon director in 2016 – the Association was critical of the company with concerns over an ongoing absence of a dividend and sustainable profit, lack of board diversity, and big bonuses. The Association asked about 6,000 shareholders for their proxy votes and received 40 million proxies on behalf of shareholders, defeating the re-election of a director.

It is also noteworthy that, in 2017, NZX promulgated its Corporate Governance Code. The Code includes a set of principles and recommendations that all Main Board listed companies must report against. The purpose of the Code is to promote good corporate governance, with a focus on long-term value. The Code is a 'comply or explain' regime.

Russell McVeagh

David Raudkivi
david.raudkivi@russellmcveagh.com

Level 30
48 Shortland Street
Auckland
New Zealand
Tel: +64 9 367 8344
Fax: +64 9 367 8596
www.russellmcveagh.com

Russia

Alexander Zharskiy, Alexander Kleschev and Kristina Akalovich
ALRUD Law Firm

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The following acts are considered as primary sources of laws and regulations relating to shareholder activism and engagement in Russia:

- the Civil Code of the Russian Federation (the Civil Code);
- the Federal Law 'On Limited Liability Companies' (the LLC Law);
- the Federal Law 'On Joint-Stock Companies' (the JSC Law);
- the Federal Law 'On Securities Market' (the Securities Market Law); and
- Resolution of the Plenum of the Supreme Arbitration Court of the Russian Federation No. 62 dated 30 July 2013 'On certain issues connected with recovery of losses by persons in the management bodies of a legal entity' (Resolution No. 62).

The Civil Code was introduced by the State Duma (one of the chambers of the Russian parliament, the Federal Assembly) and it stipulates, inter alia, the general principles of regulation applicable to all legal entities established in Russia, as well as provides for shareholders' basic rights and obligations.

The LLC Law, the JSC Law and the Securities Market Law are also acts of the State Duma. The LLC Law and JSC Law are 'special legislative acts' since they specifically cover issues related to the incorporation, operation (including, corporate governance, competence of the management bodies, decision making) and dissolution of LLCs and JSCs respectively. The Securities Market Law applies to Russian JSCs and, inter alia, regulates participation of shareholders in operation of the company, when such shareholders hold their shares through depositary (nominal shareholder).

Resolution No. 62 establishes principles of bringing the directors of a Russian company to liability for breach of their fiduciary duties.

The supervisory body for the JSCs and for any issues connected to the security markets is the Central Bank of Russia and the supervisory body for the LLCs is the Tax Service. In practice, however, enforcement of the shareholders' rights is performed directly by the shareholders in courts.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Russia may be referred to the group of countries with concentrated capital structure, in which control over a company, as a rule, belongs to one or several affiliated shareholders. Under such circumstances, the majority shareholder directly forms the management, which ensures the fulfilment of its will in the actions of the company. Therefore, an agency problem in Russia mainly arises not in a vertical ('shareholders-management') but in a horizontal section, in relations between majority and minority shareholders.

Taking into account the significant power of a majority shareholder, minority shareholders in Russia tend to be neutral or even passive in relation to the day-to-day management of the company. The Central Bank of Russia is considering how to stimulate shareholder activism and engagement at least in Russian public JSCs (Russian PJSC). In late 2017, it published a report with certain recommendations and suggestions on this issue aimed at the initiation of public hearings (available in Russian at www.cbr.ru/Content/Document/File/50695/Consultation_Paper_170925.pdf).

The involvement of social media in a conflict is, as a rule, not a preferable strategy for shareholder activism; generally, conflicts are resolved privately or with a help of court by challenging transactions of a Russian company or resolutions of management bodies.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

The Central Bank of Russia looks positively on the promotion of activists (see question 2). Based on the results of public hearings, in March 2018, a report, with a consolidated position of representatives of banks, association of professional investors and other specialists in the corporate sphere, was prepared, which, in general, showed support for the necessity of stimulating shareholder activism (available in Russian at www.cbr.ru/content/document/file/50697/comments_180305.pdf).

Where a conflict arises, the tendency is to proceed with a private settlement; however, certain activism campaigns have sometimes become public. For instance, during the past two years, the following industries have been targeted: energy (minority shareholder of Irkutskenergo PJSC v majority shareholder on pricing within tender offer), gas industry (minority shareholders of TGK-1 PJSC v Gazprom Energoholding as a majority shareholder on amount of dividends and related party transaction), retail (minority shareholders of Magnit PJSC on appointment of their nominees to the board).

4 What are the typical characteristics of shareholder activists in your jurisdiction?

Activist shareholders in Russia are usually represented by minority shareholders. Russian LLCs and non-public JSCs are characterised by a very limited number of shareholders (normally up to four shareholders), which means that shareholders usually have personal relationships with each other and have more chance to co-operate in their activism strategy. Minority shareholders of PJSCs, meanwhile, never meet each

other, inter alia, because of their large number, due to low engagement in operation of a company's business and non-attendance of general shareholders' meetings (the GSM).

Shareholders activism may be considered an effective strategy to protect interests of minority shareholders when such shareholders have a possibility to influence the decision-making process. In Russian LLCs, the vast majority of decisions are adopted by majority of votes of all the company's shareholders and, for the limited number of issues, the LLC Law establishes the two-thirds threshold or unanimity requirement. Following this, activist shareholders (acting alone or jointly) should in aggregate own at least 16 per cent of a company's share capital, in cases where 51 per cent is controlled by one or more affiliated persons. The distinctive feature of JSCs is that thresholds are determined on the basis of votes of shareholders participating in the meeting, rather than from the total number of company's shareholders' votes, that makes the prospects of affecting the decision-making process more complicated, where one or several affiliated shareholders hold a major stake.

Shareholding requirements for challenging resolutions of management bodies are described in question 10.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

As a general rule, activist shareholders are not affected by sociopolitical issues, instead they mainly scrutinise deals and transactions, resolutions and actions of management bodies, which have a direct impact on value of a Russian company (eg, major or related party transactions and transactions with key assets) or shareholding in the company.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

Activist shareholders initially try to use all informal means to reach a settlement privately (eg, informal meetings and discussions with involvement of a third party, including arbitrator, lawyer or simply a trusted person). Thus, it is not typical for Russian shareholders to make the corporate conflict public with the involvement of a wide audience and social media.

If these informal measures do not work, the next step will be enjoying their statutory corporate rights through participation in the GSM, making proposals to the agenda of a meeting, requesting information from a company or bringing claims in court as covered in more detail below.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

In general, a shareholder of a Russian company is entitled to make a proposal within the process of preparation to a GSM. In contrast to LLCs (where each shareholder has a right to make a proposal), shareholders of a JSC are entitled to make a proposal only if they hold in aggregate not less than 2 per cent of shares that carry voting rights.

Upon receipt of a shareholder's proposal, a management body authorised to convene a GSM shall, within five days of expiry of the deadline for directing the shareholder's proposals, examine the proposal and decide on its inclusion in the agenda of a meeting.

The LLC Law stipulates the exhaustive list of grounds for refusal to accept the shareholder's proposal, namely when the proposed issue:

- does not fall within the competence of the GSM; or
- does not comply with legal requirements.

The JSC Law establishes two additional grounds – a shareholder:

- missed the deadline for the proposal; and
- did not own the quantity of shares required to make a proposal.

According to the JSC Law, the shareholder must be notified on rejection of the proposal by a motivated letter within three days from the decision on rejection. The shareholder whose proposal was rejected or not included due to omission of the competent body is entitled to request the court to include its proposal in the GSM's agenda.

GSM may only be entitled to vote on issues not included in its agenda, if all shareholders of a LLC or non-public JSC attend a meeting.

Shareholder may request the company to call an extraordinary GSM outlining the proposed agenda, if a shareholder or several shareholders acting jointly own one-tenth of aggregate votes in the company.

The competent body must then decide within five days whether to convene a meeting. In the case of a positive decision, an extraordinary GSM shall be held within 40 days for JSC (or 75 days if GSM's agenda includes an item on appointment of members of a board of directors) and 45 days for LLC from the date of receipt of a shareholder's requirement to call a meeting.

The authorised management body is entitled to refuse convening a meeting only if: (i) a shareholder violated the procedural requirements; or (ii) the proposed issues does not fall within the competence of GSM. Where a negative decision or no decision has been adopted, a shareholder (or shareholders), who requested a meeting, in the case of a LLC – is entitled to convene a meeting by itself and in the case of JSC– is entitled to claim in court for such a company to hold a meeting.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Shareholders of a Russian company may nominate their candidates to be appointed to the board at GSM convened in accordance with the procedure described in question 7. In a Russian JSC, such right belongs only to a shareholder (shareholders) who holds in aggregate not less than 2 per cent of shares that carry voting rights, while in LLCs no thresholds are established.

The shareholders may agree in the company's charter to apply the cumulative voting system for the election of board members that strengthen the ability of minority shareholders to elect a director.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Shareholders may call an extraordinary (special) GSM in accordance with the procedure described in question 7.

GSM can be held in the form of voting in person or absentee voting without holding a meeting with prior submitting of voting ballots (Russian law establishes certain restrictions on issues of the agenda which cannot be resolved by absentee voting). In the latter case, the voting may be performed by the exchange of documents through postal, telephone, electronic or any other communication that ensures the authenticity of transferred and received messages and their documentary confirmation.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Shareholders are entitled to initiate, inter alia, the following types of civil actions against a Russian company and its management bodies:

- challenging resolutions of company's management bodies;
- bringing a claim to the court to procure JSC convening the GSM (in cases described in question 7);
- challenging company's transactions; and
- claiming for compensation of damages caused by controlling persons (as defined in question 11) to the company due to the actions (omissions) in breach of fiduciary duties.

In the context of challenging the GSM's resolutions, claims may be brought only by those shareholders who voted against or did not participate in the GSM in question.

For shareholders of JSCs to bring a claim in court against company's management bodies, the claiming shareholder (or several shareholders acting jointly) shall hold in aggregate not less than 1 per cent of issued ordinary shares of the company.

Following civil law reform that took place in Russia in 2014 the shareholders have been granted with a right to bring derivative actions acting on behalf of a Russian company in cases set out in questions 3 and 4. Resolution of the Plenum of the Supreme Court of the Russian Federation No. 25 dated June 23, 2015 additionally clarified that where litigation is successful, the damages caused to the company are awarded in favour of the company, shareholders in such cases act as company's representatives.

Group actions (akin class actions) may be initiated by shareholders in accordance with the rules of Chapter 28.2 of the Arbitral Procedural Code of the Russian Federation. However, this instrument is not widely used in practice, since the minimum number of shareholders should be five, while, for shareholders of Russian LLCs and JSCs with concentrated capital structure, it is more practical to initiate an action with multiple claimants having their own individual claims. At the same time, it can be expected that minority shareholders of PJSCs will tend to use group actions to protect their interests due to apparent difficulties in reaching the 1 per cent threshold to initiate a litigation in situation of dispersed shareholding in PJSCs.

For the purpose of preparing for a litigation, the shareholders can use publicly available information (especially information disclosed by PJSC) and use their information rights under corporate law as described in question 26.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

According to the Civil Code, a person who has a right to represent a company or has actual possibility to direct company's actions as well as members of collegial management bodies (the controlling persons) shall act reasonably and in good faith in best interests of the company and may be liable for damages caused to the corporation for their fault.

No exhaustive list of criteria for finding a person as having actual possibility to direct company' actions is officially stipulated; however, in general, this wording includes shareholders, who have control over the company or have a right to give mandatory instructions to a person, who has a right to represent a company or to members of collegial management bodies. Normally, activist shareholders are not included in this category, as they usually do not have substantial influence on a company's operation.

In the meantime, each shareholder (including minority shareholder) of a Russian company has legally established obligations, inter alia, it shall not commit actions intentionally aimed at causing damage to the company and shall not commit actions (omission)that obstruct or make it impossible to achieve the objectives for which the company was established. These obligations are not formally deemed to be fiduciary duties, however, they are similar in nature.

Compensation

12 May directors accept compensation from shareholders who appoint them?

Russian companies are managed by, inter alia, a chief executive officer (the CEO), which represents the company and acts on its behalf without power of attorney in relations with third parties, and a board of directors, which, except for certain cases, is an optional management body.

The CEO should obligatory enter into an employment agreement with a company and receive a salary and other bonus payments (if any) from it. At the same time, there is no statutory requirement for the members of the board to be employed by a Russian company or to be remunerated for performance of services in their capacity as directors. However, shareholders may decide on establishment of remuneration to be paid to the members of the board by a Russian company. It is not typical for shareholders in Russia to pay any fee directly to the director appointed by the shareholders.

Mandatory bids

13 Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

Bid requirements apply only to Russian PJSCs. If a person or persons acting in concert (whether being a shareholders or not) intend(s) to acquire in aggregate more than 30 per cent of the shares that carry voting rights, they are entitled to make a voluntary tender offer (VTO) to acquire the reminder of the shares. While if a person or persons acting in concert acquired more than 30, 50 or 75 per cent of the voting rights, they are obliged to make a mandatory tender offer (MTO) to acquire the reminder of the shares.

Shareholders are considered to be acting in concert if they are affiliates.

In cases where, following the results of the VTO or MTO, a person solely or together with its affiliates acquired more than 95 per cent of voting rights of a Russian PJSC, such person: (i) shall acquire the reminder of the shares upon request of the remaining shareholders or (ii) is entitled within six months from the date of acceptance of the VTO or MTO to demand from remaining shareholders to sell their shares, provided that not less than 10 per cent of the shares have been acquired by way of VTO or MTO.

Disclosure rules

14 Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Shareholders of a PJSC have obligation to disclose their shareholding or intentions to acquire shares of PJSC in cases described in question 13. Russian PJSCs also have an obligation to disclose as a material fact on

their websites information on acquisition or termination of a person's right to directly or indirectly dispose of a certain number of votes attributable to voting shares, if the number of votes is 5 per cent or became more or less than 5, 10, 15, 20, 25, 30, 50, 75 or 95 per cent of the total number of votes attached to the company's voting shares.

In addition, pursuant to the JSC Law affiliates of the company shall inform the company in writing on number and types of shares acquired by them in such company not later than 10 days following the date of acquisition. Affiliates of the company are determined in accordance with rules established in Law of the RSFSR 'On Competition and Restriction of Monopolistic Activity in Trade Markets'.

With respect to Russian LLCs, the company should be notified on disposal of shares in its share capital within three days from the date of notarial certification of the agreement, aimed to disposal of Russian LLCs share.

It should be noted that, under the Federal Law 'On Protection of the Competition', acquisition of shares in a Russian LLC or JSC may be subject to merger clearance control with Russian Federal Antimonopoly Service if certain thresholds with respect to worldwide value of assets or worldwide aggregate turnover of the purchaser and the target Russian company are met.

Further, acquisition by a foreign investor of shares or other forms of control (both direct and indirect) in respect of a Russian company engaged in activities that are recognised as having strategic importance for the national defence and security (strategic companies) might be subject to clearance by the purchaser under Federal Law 'On Procedures for Making Investments in Commercial Entities of Strategic Importance for Defence Support and National Security' (the Strategic Investments Law). The list of the strategic activities is contained in article 6 of the Strategic Investments Law. It should be noted that the Russian Governmental Commission (which oversees foreign investments into strategic businesses) presided over by the Russian Prime Minister is entitled to escalate any transaction by a foreign investor to the strategic clearance process, which otherwise only applies to investments into strategic companies.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

The Central Bank of Russia prescribes that JSCs shall disclose information to the repository on commencement of transactions with derivative instruments in cases where consideration under such transaction (series of transactions) meets certain thresholds.

Where one of the parties is a credit institution, insurance company, broker (or a company of certain other type), transactions with derivative instruments should be disclosed in all cases (irrespective of their value).

Insider trading

16 | Do insider trading rules apply to activist activity?

In accordance with the Federal Law 'On Countering the Illegal Use of Inside Information and Market Manipulation' (with amendments that will come into force on 1 May 2019), among others, (i) a person who directly or indirectly (through its controlled persons) holds not less than 25 per cent of votes in companies specified in such law and (ii) a person that have access to inside information under federal laws, constitutional document or internal documents by virtue of owning shares in companies specified in such law are deemed to be insiders.

Following this, an activist shareholder, who will unlawfully use inside information of a Russian company or will manipulate the market for the purposes to achieve its objectives, will be subject to liability under legislation of the Russian Federation.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

In all cases, including in the context of an activist's proposal, the directors, including CEO, owe duties to act reasonably and in good faith in the best interests of the company. Whatever the activist shareholder proposes to the management bodies, the directors shall always review the proposal from the point of possible damages and negative effects to be caused to the company as a result of implementation of such proposal.

Resolution No. 62 stipulates standards for evaluation of directors' actions by a court and establishes certain rebuttable presumptions with respect to actions that are a priori considered to be unreasonable or taken in bad faith, which are not applicable while considering activist's proposals on their compliance with shareholders' obligations to a company.

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

The most appropriate strategy for the company is to monitor any tension in relations between the shareholders as well as between shareholders and management, analyse the most conflict areas and potential reasons behind contradictions in order to be able to ex ante react on activist shareholders' actions.

A number of Russian JSCs have already established special committees on interaction with minority shareholders and on corporate governance that act under control of a board of directors. It is likely that these will be adopted by other Russian companies as best practice.

Defences

19 | What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Russian companies, being mainly controlled by one or several affiliated persons with strong corporate powers, already have a certain level of protection due to their concentrated capital structure.

However, additional measures can be taken to strengthen the company's position and preclude situations of being involved in activism strategies of its shareholders, inter alia: (i) management bodies of the company or specifically established committees may perform constant monitoring of the most sensitive for shareholders areas of company's activities and (ii) justified reports of the company's management on reasons behind certain decisions of the management bodies may help decrease the number of cases of challenging the company's transactions or resolutions of its bodies.

Where a shareholder activism has already taken place, the recommended strategy is to attempt to de-escalate the conflict by settlement through informal communications, meetings, sessions between activist shareholders and management bodies.

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

Where a shareholder is not able to attend a meeting personally, it is entitled to grant a power of attorney to its representative or participate through electronic means of communications as described in question 25. Voting by way of ballots is permitted only for meetings held in the form of absentee voting, when no shareholders are present at the meeting.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

As described above, the conflicts between shareholders and between shareholders and management bodies are primarily resolved by negotiations and private settlement, if such means allow escalating the conflict. According to the Code of Corporate Governance enforced by the Central Bank of Russia as a source of soft law applicable to PJSCs, the company is obliged to take all necessary and possible measures to prevent and resolve the conflict (as well as minimise its consequences), including using extrajudicial procedures of dispute resolution, including mediation.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

The obligation of management bodies to inform all the shareholders on a GSM, with the possibility for shareholders who comply with threshold requirements as described in question 7 to make proposals to GSM's agenda, can be considered as the key engagement effort of the company with respect to its shareholders. Russian bid requirements described in question 13 also stimulate the organised involvement of shareholders.

23 Are directors commonly involved in shareholder engagement efforts?

Normally, the activist shareholders communicate with the company's CEO and (subject to certain restrictions connected with their shareholding in JSCs) with directors on the issues falling within their competence, as well as with chief financial officer and other key employees of a company.

According to the Code of Corporate Governance, the board of directors should play a key role in preventing, identifying and resolving internal conflicts between the company's management bodies, shareholders and the company's employees ensuring the effective protection of shareholder's rights if they are breached. At the same time, it is not recommended for a director, who is or potentially may be affected by the conflict, to participate in the work of a board of directors aimed at the resolution of such a conflict.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Russian companies are not obliged to disclose any shareholder engagement efforts; however, the charter of the company may stipulate a press and a company's website or solely the company's website as additional sources for informing shareholders on holding a GSM.

Where shareholders want to communicate directly with directors, they may use both formal (eg, serving a written request through the company) and informal means of communication in the interest of time and operative interaction (eg, personal meetings, through special services in a personal account on a company's website).

As a guidance principle, the company must ensure equal and fair treatment of all shareholders in the exercise of their right to participate in the management of the company, which means that a company is not allowed to disclose information to its shareholders selectively or unequal. In the meantime, according to the Code of Corporate Governance, when a company provides information to shareholders, it is recommended to ensure a reasonable balance between the interests of certain shareholders and the interests of the company itself, which is interested in maintaining the confidentiality of important commercial information that may have a significant impact on its competitiveness.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

Russian law requires that all communications between a company and its shareholders shall be made in the form of notices prepared in writing and delivered at the address of a shareholder set out in the list of shareholders or shareholders register. In addition to the alternative sources of communication described in question 24, the company may use emails and text messages, if it is provided by the company's charter.

Votes of shareholders may be solicited by way of voting ballots (for absentee voting), personal attendance or participation of a shareholder's representative acting by virtue of a power of attorney. In the Code of Corporate Governance, it is also recommended to create special systems that allow electronic voting, for instance, through a personal account on the company's website or special platforms for e-voting via the internet, provided that sufficient reliability, identification and protection is provided. Online voting has already been experienced, for instance, by shareholders of Sberbank of Russia, Rostelecom and MGTS in 2018.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

The list of registered shareholders of a Russian LLC and information on their shareholding is publicly available and may be obtained through online service supported by Russian tax authorities. Moreover, as rule, a list of shareholders with their addresses, shareholding percentages is kept by LLC itself.

Russian JSCs are more confidential in this respect. There is no obligation for the shareholders or a Russian JSC itself to provide the Russian tax authorities with an update on changes in shareholders or their shareholding. The up-to-date register of shareholders is maintained by the registrar acting on the basis of an agreement with a Russian JSC. Information on (commercial) name of shareholders registered in a shareholders' register and number of their shares may be requested from the registrar and obtained only by a shareholder owning more than 1 per cent of shares in respective company. Where shares of JSC are held through a nominal shareholder, actual (beneficial) owners are not disclosed by the registrar to such requesting shareholder.

Except for certain legally established exclusions, Russian companies are also obliged to collect and keep the information on their beneficiaries. For this purpose, beneficiary is determined as a natural person, who directly or indirectly (through third persons) owns (holds more than 25 per cent of a share capital) of a legal entity or has a right to control its activities. Disclosure of such information is required only in cases expressly prescribed by law.

In addition, certain information on the company and its activity should be disclosed to a shareholder upon its request, which complies with certain requirements. In contrast to LLCs (where all shareholders have equal information rights), shareholders of JSCs enjoy different information rights depending on their shareholding in the company:

- not less than 1 per cent, but less than 25 per cent; and
- not less than 25 per cent of shares that carry voting rights.

For the first indicated group of shareholders of JSCs, the JSC Law sets out an additional requirement to stipulate the business purpose of a shareholder's request of information.

The requested documents shall be provided by a company to its shareholder, as a rule, within five business days for LLCs and within seven business days for JSCs from the date of receipt of a shareholder's request.

The grounds for when a Russian company is entitled to refuse access to documents and information are:

- an electronic version of the requested document is in public domain;
- the document is repeatedly requested within three years, provided that the first request was properly satisfied by the company;
- the document pertains to the periods over three years before the time of request (with limited exceptions);
- no business purpose is specified (if it is required under the JSC Law);
- a shareholding threshold requirement is not met; and
- the document pertains to the time periods when a respective shareholder did hold shares of a Russian JSC.

Where the company fails or refuses to provide the requested information without formal grounds to do so (as described above), shareholders are entitled to claim the provision of information from the company in court.

It should be noted that a PJSC has an obligation to disclose certain information on its website, including financial accounts, charter of a company and its internal regulations in respect of operation of its management bodies, information on affiliates, which are publicly available.

ALRUD

Alexander Zharskiy
Alexander Kleschev
Kristina Akalovich
info@alrud.com

17 Skakovaya Street
Building 2, 6th floor
125040 Moscow
Russia
Tel: +7 495 234 96 92
Fax: +7 495 956 37 18
www.alrud.com

Switzerland

Mariel Hoch
Bär & Karrer Ltd

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

The primary sources of laws and regulations relating to shareholder activism are the Swiss Code of Obligations (CO) governing the rights and obligations of companies' boards of directors and shareholders in general and the Swiss Financial Market Infrastructure Act (FMIA), enacted on 1 January 2016, containing additional rules for listed companies and their shareholders. The provisions of the FMIA are set out in more detail in two ordinances, the Swiss Financial Market Infrastructure Ordinance (FMIO) and the Swiss Financial Market Infrastructure Ordinance by FINMA (FMIO-FINMA). Further, the Ordinance against Excessive Compensation in Listed Companies (OAEC) contains specific rules on the compensation of management and board of directors. The Takeover Ordinance (TOO) sets out detailed rules on public takeover offers including boards' and qualified shareholders' obligations. Companies listed on the SIX Swiss Exchange are also bound by, inter alia, the Listing Rules (LR-SIX), the Directive on Ad hoc Publicity (DAH) and the Directive on Information relating to Corporate Governance (DCG).

The CO and FMIA are enacted by the national parliament, the FMIO and the OAEC by the Swiss Federal Council, the FMIO-FINMA by the Swiss Financial Market Supervisory Authority FINMA (FINMA), the TOO by the Swiss Takeover Board and the LR-SIX as well as the DAH by SIX Exchange Regulation.

Compliance with the CO and the OAEC is primarily enforced by the civil courts. FINMA enforces the FMIA as well as its ordinances and the Takeover Board enforces the TOO and the takeover related provisions of FMIO-FINMA. Compliance with the LR-SIX, DAH and DCG is enforced by the SIX Exchange Regulation.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Compared with other jurisdictions, in particular the United States, the number of activist campaigns involving Swiss companies is still moderate. However, with about 35 shareholder actions between 2010 and 2018, Switzerland is a key European target for activist shareholders. Since 2012, actions in Switzerland have more than doubled. The chances of success depend on the content of the campaigns and cannot easily be measured among others because targets may announce changes in operations or strategic adjustments as their own (pre-existing) plans that happen to coincide with the requests of the activist shareholder. Proxy fights at shareholders' meetings are rarely successful, but occasionally activists win them. The chances of success are higher if proxy advisers such as ISS and Glass Lewis issue voting recommendations in support of the activist's requests.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

The corporate community is generally critical of shareholder activism due to its short-term orientation. The legislator and regulators have not expressed a position on shareholder activism but tend to lower the hurdles of shareholder minority rights. Retail shareholders and the general public will form an opinion on a case-by-case basis. Institutional shareholders will analyse the requests of the activists and decide whether or not to support them. Only in rare instances, will they vote with the activist.

It seems as though basic materials, technology and services are regularly targeted industries; the financial industry, industrial goods and the healthcare sector have also attracted interest from activists. Due to a variety of reasons that have attracted activist shareholders in the basic materials industry, it should not be concluded that this industry is particularly prone to activist campaigns. Also, there are no regulatory reasons that facilitate shareholder activism in certain industries over others.

In Switzerland, four shareholder activists have recently been engaged in campaigns; namely, (i) the US-based investment fund Third Point with its founder Daniel Loeb acquired 1.3 per cent in Nestlé at the end of June 2017; (ii) the investor group White Tale Holdings acquired a stake in Clariant and then in July 2017 increased the stake to more than 20 per cent and successfully prevented the merger between Clariant and Huntsman and eventually exited its investment by selling its stake to the Saudi chemical firm SABIC International Holdings BV; (iii) RBR Capital Advisors with its manager Rudolf Bohli acquired a stake of 0.2 to 0.3 per cent in Credit Suisse and requested that Credit Suisse be split in three businesses, that is, an investment bank, an asset manager and a wealth management group; and (iv) Veraison requested at the AGM 2019, inter alia, a change in the board composition at Comet Holding AG.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

Swiss public companies have been mainly targeted by international hedge funds, but Swiss hedge funds have also engaged in a number of situations.

Although it is hardly possible to make a general statement regarding the short- or long-term orientation of the inhomogeneous group of activists present on the Swiss market, it is probably fair to say that they are naturally rather mid- to long-term oriented. Typically, activist shareholders aim at giving all supporting shareholders a voice

at the board table. They may raise different issues that ultimately ensure companies are managed in their owners' interests (whether short- or long-term interests). However, there has been an increasing level of more contentious activist interests in recent years. These activists are focused on ensuring that any value being invested for the long-term benefit of the company is immediately released for the investing public (eg, by cutting investments with long-term returns, closing or spinning off separable divisions or increasing payout ratios). There is no clear pattern as to whether traditional large shareholders support activists in their endeavours. This partly depends on whether the activists benefit from the recommendations of leading proxy advisers.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

Shareholder activism in Switzerland primarily focuses on governance issues (particularly board representation and executive compensation) as well as on strategic and operational matters (particularly dividends and divestitures). Activist shareholders usually seek a (stronger) representation in the board of directors. It is estimated that in Switzerland activists use board representation as a tactic more than anywhere else in Europe. In particular, the implementation of the OAEC has led to increased attention placed at executive compensation-related governance issues: activist shareholders have a binding vote on the executive compensation of the Swiss company's executive management – one of the most powerful tools to direct the management's conduct. It is worth noting, however, that it is extremely rare that shareholders reject the compensation submitted to them by the board of directors.

By way of contrast, social activism is rarely tabled in any activist campaigns. However, there are certain indications that sociopolitical matters such as board gender diversity or the disclosure of political spending and lobbying could play a role with regard to governance activism in the future.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

Shareholder activism normally starts with building up a relatively small stake of shares avoiding triggering the disclosure obligations pursuant to the FMIA (especially the first threshold of 3 per cent). Prior to increasing its stake, a common activist will make private contact with the company's executive management or board representatives in order to present and discuss its ideas and specific demands. These private negotiations are also the reason why it is believed that almost 50 per cent of all activist campaigns never become public. However, attention should be paid to the duty of equal treatment of all shareholders and the duty of ad hoc publicity.

If the private negotiations fail, an activist may launch a public campaign to divulge the key requests towards the company and, by doing so, obtain the support of other shareholders (since shareholders do not have a right to access the share register, the only way of reaching out to other shareholders holding less than 3 per cent is through the media). As psychology plays an important part in the fight for control, gaining the support of the public opinion is a crucial element in winning the battle. The share price is likely to increase following the publication of the key elements of the campaign as it is likely to attract new investors. In the run-up to the shareholders' meeting, the composition of shareholder base of the target company may change towards increased support of the activist's campaign. Based on the public support and also depending on the support from professional proxy advisers, the activist shareholder may be in a position to find an attractive compromise with the board.

Fruitless settlement attempts may lead to proxy fights at and outside the shareholders' meeting (including the enforcement of the information rights, freezing entries in the commercial register and challenging allegedly non-compliant shareholders' resolutions) or even result in litigation (eg, liability claims) and criminal charges.

Ahead of the shareholders' meeting the activist shareholder may decide to form a group with one or more other key shareholders. According to the FMIA, any person who reaches, exceeds or falls below 3, 5, 10, 15, 20, 25, 33.3, 50 or 66.6 per cent of the voting rights of the target company must notify the target company and the stock exchange (the SIX Disclosure Office for SIX listed companies). The activist may use such disclosure as signal of determination to the company and financial markets. It typically also triggers an additional round of media reports.

Although irrelevant to win a proxy fight but helpful to the communication strategy, the activist shareholder often uses the shareholders' meeting to speak publicly and reiterate their requests for improved performance.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

All shareholders have the right to attend shareholders' meetings, the right to vote and to request information and inspect documents (to the extent company interests requiring confidentiality do not prevail). The right to information is regularly used by activist shareholders to increase pressure prior to shareholders' meetings. The board is obliged to respond to such questions during the shareholders' meeting. All shareholders have the right to propose motions and counter-motions (eg, regarding board elections) at shareholders' meetings and may request a special audit or a special expert committee to investigate certain facts and behaviours of the board or management.

Furthermore, any shareholder (or group of shareholders) representing shares of a par value of at least 1 million Swiss francs (the articles of association may contain a lower threshold) is entitled to demand that certain agenda items be tabled at the next shareholders' meeting. Any shareholder (or group of shareholders) representing 10 per cent of the share capital (again, a lower threshold may be contained in the articles of association) may request that an extraordinary shareholders' meeting be convened. According to the predominant legal doctrine, these thresholds should be regarded as alternative criteria (ie, shareholders representing 10 per cent of the share capital are also entitled to put forward an agenda item and shareholders representing shares of a par value of at least 1 million Swiss francs may call an extraordinary shareholders' meeting).

The current draft for a revision of Swiss corporate law suggests the thresholds for shareholders to benefit from certain minority rights (eg, to request items to be added to the agenda) should be lowered. The revision has not yet been passed into law.

In cases where a shareholder demands that an agenda item be tabled for the next shareholders' meeting, the respective deadline for such submissions is contained in the articles of association and ranges typically between 40 and 55 days prior to the meeting. The company is obliged to include the item and the shareholders' motion relating thereto in the invitation to the shareholders' meeting. The board will add its own motion to such item.

Shareholders representing at least 33.3 per cent of the voting rights may block special resolutions (capital transactions, mergers, spin-offs, etc), shareholders holding at least 50 per cent of the voting rights may force ordinary resolutions (eg, appointment of a director)

and shareholders representing at least 66.6 per cent of the voting rights may force special resolutions (eg, amendments to the articles of association). As these thresholds typically relate to the total votes represented at the shareholders' meeting and given that shareholder representation typically ranges between 45 and 65 per cent, the shareholdings required to pass the aforementioned thresholds are much lower.

Under the CO and OAEC, a number of corporate decisions such as the amendment of the articles of association, capital increases, the approval of the annual accounts and resolutions on the allocation of the disposable profit, the election of board members, the chairman and the members of the compensation committee as well as board and management compensation fall into the mandatory competence of the shareholders' meeting. According to the OAEC, elections (or re-elections respectively) of board members must take place annually and elections must take place individually. Therefore, activist shareholders aiming at deselecting members of the board of directors are not required to request an extra agenda item for this purpose, but may simply vote against the re-election tabled by the company.

Except for the request for an extraordinary shareholders' meeting or a special audit and the appointment of an auditor at the request of a shareholder, it is not possible to request that additional agenda items be tabled during the shareholders' meeting. However, any shareholder may make motions relating to any agenda item during the shareholders' meeting. This is particularly relevant with respect to any election items as additional persons may be proposed for election. Against the background that a significant number of shareholders cast their votes via the independent proxy without giving specific instructions as to ad hoc motions (or by instructing the independent proxy to follow the board's recommendation in such case), ad hoc motions generally have a low likelihood of succeeding.

Other than with respect to the number of votes or percentage of the capital, Swiss law does not distinguish processes depending on the type of shareholder submitting a proposal.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Any shareholder is entitled to nominate a director for election to the board, usually as a motion within the agenda item 'election of the members of the board of directors'. In this context, if the motion is filed with the company in a timely fashion, the board is obliged to publish the shareholder's motion in the company's invitation to the shareholders' meeting at the company's expense. However, shareholders may not directly access the share register and divulge their requests via a special proxy access tool.

Activists typically use the media or a dedicated web page for their campaigns once their intentions are publicly disclosed.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Any shareholder – individually or acting in concert – representing 10 per cent of the share capital (or, according to the predominant legal doctrine, representing shares of a par value of at least 1 million Swiss francs; see question 7) has the right to call an extraordinary shareholders' meeting. Certain companies have introduced lower thresholds in their articles of association. The required threshold may also be reached by several shareholders acting in concert. The request to call an extraordinary shareholders' meeting must be submitted in writing to the company's board and must contain the requested agenda items including the activist's motions thereto.

Shareholders may not act by written consent in lieu of a meeting, but they can be represented by issuing written voting instructions to either the independent proxy or (depending on the articles of association) to another shareholder or a third party.

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Shareholders may in principle not file lawsuits on behalf of the corporation or on behalf of all shareholders. However, they may file liability actions against directors and members of the executive management where the payment of damages is directed to the company. In addition, any shareholder may challenge shareholders' resolutions made in violation of the laws or the articles of association with effect for the entire company. Also, certain post-M&A appraisal actions under the Swiss Federal Merger Act have erga omnes effect (ie, all shareholders in the same position as the claimant receive the same compensation). The cost of such proceedings must generally be borne by the company (ie, the defendant).

In general, class actions are not specifically addressed in the Swiss civil procedure. Nevertheless, it allows for a joinder of plaintiffs or defendants: several parties may join their lawsuits in case the same court has jurisdiction and all claims are based on the same set of facts and questions of law. This approach reduces costs and avoids conflicting judgments, but increases complexity. Another corporate litigation tactic worth noting is launching a single litigation test case in order to have a precedent for multiple actions involving the same set of facts and questions of law.

Shareholders are not able to directly prevent the company from accepting a private settlement with an activist shareholder. They may only challenge the board's settlement resolution on the grounds that such decision was void or bring liability actions against the directors should the board have breached their directors' duties and should they have caused damage to the company by doing so.

Every shareholder has the right to request information and to inspect documents (to the extent company interests requiring confidentiality do not prevail). The right to information is regularly used by activist shareholders to increase pressure prior to shareholders' meetings. The board is obliged to respond to such questions during the shareholders' meeting (see question 7).

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

Shareholders, including shareholder activists holding a significant or majority stake, do not owe any fiduciary duties or duty of loyalty to the company. They may in particular cast their votes in their own (short term) interest irrespective of whether such interests are contrary to the company's long-term interests.

Compensation

12 | May directors accept compensation from shareholders who appoint them?

There is no Swiss law or regulation preventing shareholders from paying direct compensation (ie, remuneration in addition to the compensation bindingly resolved by the shareholders' meeting) to their directors. However, the shareholders may not derive any special rights from this contribution as the directors are always obliged to act in the best interest of the company (duty of loyalty to the company) and generally to treat all shareholders equally. The board member will need to disclose and handle resulting conflicts of interest according to the company's regulations and the company may have to disclose the compensation in the annual report and pay social security contributions on all such amounts.

Mandatory bids

13 | Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

Shareholders acting alone or in concert with other shareholders with the intention to control the relevant company are obliged to launch a mandatory bid if they exceed the threshold of 33.3 per cent of the voting rights of a listed company. The articles of association of a company may raise the relevant threshold up to 49 per cent of the voting rights (opting up) or may put aside the duty to launch a takeover offer completely (opting out). Shareholders are deemed to act in concert with respect to the mandatory bid obligation if they (i) coordinate their behaviour, (ii) by contract or other organised procedure or by law, and (iii) this cooperation relates to the acquisition or sale of shareholdings or exercising of voting rights.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Any shareholder or group of shareholders acting in concert must disclose if it attains, falls below or exceeds the threshold percentages of 3, 5, 10, 15, 20, 25, 33.3, 50 or 66.6 of the voting rights of the company (irrespective of whether the voting rights may be exercised or not). This applies to direct or indirect holdings of shares as well as to the holding of financial instruments with such shares as underlying. Shareholders are considered to be acting in concert if they are coordinating their conduct by contract or by any other organised method with a view to the acquisition or sale of shares or the exercise of voting rights.

The disclosure entails the number and type of securities, the percentage of voting rights, the facts and circumstances that triggered the duty to disclose, the date the threshold was triggered, the full name and place of residence of natural persons or the company name and registered seat of legal entities as well as a responsible contact person. The shareholder's intentions must not be disclosed.

The disclosure must be made towards the company and the stock exchange within four trading days following the triggering event. The company must publish the required information within another two trading days.The maximum fine that may be imposed on non-reporting parties amounts to 10 million Swiss francs in case of intentional conduct and 100,000 Swiss francs in case of negligence. The Federal Department of Finance (FDF) is the competent authority to issue such fines. In most instances, the FDF commences its procedures following a criminal complaint made by FINMA.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

The disclosure requirements apply to all derivate instruments (eg, conversion rights, option rights, etc) and long as well as short positions need to be disclosed. In addition, if shareholders are acting in concert (see question 14 with respect to mandatory bid rule), their shareholdings or holdings of derivate instruments are aggregated and they need to make the disclosure as a group. For purposes of the notification of significant shareholdings parties are deemed to act in concert if they (i) coordinate their behaviour, (ii) by contract or other organised procedure or by law, and (iii) this cooperation relates to the acquisition or sale of shareholdings or exercising of voting rights.

Insider trading

16 | Do insider trading rules apply to activist activity?

Insider trading rules apply to activist activity; that is, if the intentions of the activist shareholder are deemed as inside information, the activist shareholder may not communicate such information to anyone, including other shareholders, prior to making it public unless the communication to other shareholders is required to comply with legal obligations or in view of entering into an agreement. An activist wanting to purchase shares in a company does not constitute insider trading. As the campaign typically includes more than just the purchase of target shares (eg, change in board composition, request of corporate actions), activist shareholders need to carefully structure their campaign and the building up of their stake in order to avoid risks of insider trading.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

Directors must apply the same standard of care to an activist proposal as to any other proposal or matter. They have to act and resolve in the best interest of the company and must treat all shareholders equally under equal circumstances. Also, board members (formally or informally) representing a shareholder on the board of directors must appropriately deal with their conflicts of interests when facing their shareholder's activist campaign.

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

As shareholder activism has gained traction in Switzerland, larger listed companies are investing more time and resources in activist engagement in order to deal with activists' concerns appropriately. Accordingly, the preparation and implementation of preventive as well as defending measures against activists' attacks have become part of a corporation's routine. This increased attention may be regarded as an impact resulting from shareholder activism.

Preventive measures minimise the risk of a campaign. In particular, the board may identify and reduce existing exposures of the company to activist shareholders. As a first step, the board will examine the company's exposure and analyse issues that are likely to be addressed by an activist investor. Key features of an exposed company are, inter alia:

- undervaluation (which can be addressed by value-adding sale possibilities of separable divisions or non-core assets);
- board instability (especially decreasing support by the shareholder base);
- large cash reserves combined with a comparably low dividend payout ratio; and
- M&A transactions involving the company.

Additionally, the executive management should continuously monitor and assess the company's shareholder base to identify potential shareholder activists. At this stage, the board may also consider appointing a (stand-by) task force comprising specialists in public relations, finance and law. However, even if the board manages to implement effective preventive measures, a complete elimination of the risk of becoming a target of activists is – in light of the various activists' interests – not possible.

Once an activist investor emerges and expresses its concerns to the company's board, which usually occurs in a private setting at first, the board should be in a position to revert to a set of prepared tools. First, a board is well advised to listen open-mindedly and attempt to engage politely in a constructive dialogue with the activist investor addressing and considering the activist's legitimate concerns. Following a close examination of the issues raised, the dialogue should continue and a dismissive or confrontational stance should be avoided. Consistency in the board's engagement is important to preserve credibility.

Where no satisfactory solutions can be reached during the private conversations, the board may revert to its defence tools that include:

- responding clearly and comprehensively to the activist (ignoring the issues addressed is usually not an option):
- using committed and consistent board communication (direct and public engagement with the shareholders, especially by issuing a White Paper illustrating the company's position); and
- engaging in dedicated dialogue with the company's major shareholders and significant proxy advisory firms (in order to secure their support).

The company may be able to identify an investor who would go public in support of the board. An approach that has proven effective in past activist campaigns is to slightly relent towards the position of the activist with a moderate alternative proposal in order to steal the activist's thunder.

As a long-term defence measure, some target boards consider gaining a friendly long-term anchor shareholder who is supportive of the current board's strategy.

Defences

19 What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

The potential target company may implement a set of defensive measures, particularly defensive provisions in the articles of association concerning, inter alia, transfer restrictions, voting rights restrictions (3 and 5 per cent are the most common thresholds), super voting shares (ie, shares with a nominal value reduced by up to 10 times by keeping the one-share, one-vote principle, normally assigned to an anchor shareholder) and super majorities relating to specific resolutions or to a quorum at the shareholders' meeting. Such structural defences may be an efficient tool to hinder short-term interested shareholders. In addition, Swiss regulation already provides for certain effective impediments an activist must overcome including, especially, the disclosure requirements (see question 7) and the mandatory tender obligation (at 33.3 per cent) pursuant to the FMIA as well as the lack of access to the company's share register. It is a difficult balancing act for the activist to engage in conversations with other shareholders and to avoid triggering disclosure obligations or even a mandatory bid obligation due to an acting in concert. Target boards will sometimes use this legal risk to destabilise the activist shareholder and shareholders showing sympathy with his or her actions.

A structural feature that makes a corporation more likely to be the target of shareholder activism is, in particular, the implementation of an opting-out clause (or an opting-up clause, respectively) regarding mandatory bid obligations. The release of an investor building up a majority stake from the duty to launch a public tender offer means an elimination of a main legal impediment that activists face in Switzerland.

Although not picked up by the recently published draft revision of Swiss corporate law, criticism with respect to the instruments of super voting rights and opting out has been voiced in relation to the ongoing battle for control over Swiss listed company Sika.

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

In general, the company itself is not entitled to request to receive and review proxy forms returned to the independent proxy or proxy advisory firms (see question 2) prior to the shareholders' meeting. However, proxy advisers tend to get in contact with the company (if the company has not itself reached out to the proxy advisers) to discuss their voting recommendation prior to releasing them. This dialogue with proxy advisers gives the company a rough indication of how votes might be cast at the shareholders' meeting.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

The entering into settlements with activists is rare in Switzerland. One example was the settlement of the board of directors of gategroup Holding AG with RBR Capital Advisors during a proxy fight where the parties agreed on the composition of the board of directors.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

Joining forces with regard to an activist campaign is rather uncommon. By reference to a recent case, RBR Capital and the London-based hedge fund Cologny Advisors have formed a shareholder group that controlled more than 10 per cent of the Swiss public company gategroup Holding AG.

Organised shareholders customarily conclude a shareholder agreement at first to outline their joint concerns and plan of action. Such agreements typically entail voting commitments regarding shareholders' meetings, how to handle disclosure notification issues pursuant to the FMIA (disclosure only needs to be made by one member of the group), provisions to avoid triggering the mandatory bid obligation (see question 20), a communication policy and confidentiality obligations. Such jointly organised engagement allows shareholders to publicly announce their group with a joint approach, which can increase the pressure on the company. Even without a formal shareholder agreement, the acting in concert of several shareholders is likely to trigger

disclosure obligations. Swiss law does not provide for any formal requirements in how activist shareholders must approach the company. Depending on their campaign strategy and their general policies, they will either engage with the company in confidential conversations or take the public route (which is typically preceded by confidential discussions). The levels of success of these approaches depend on the specific characteristics of target including the industry it belongs to.

23 Are directors commonly involved in shareholder engagement efforts?

Once the initial private conversations between the activists and the target company turn out to be fruitful, it is common to contractually fix the framework conditions regarding the further approach (eg, relating to a supported board representation). It is common for activists to approach not only the chairman of the company's board but also those board members they already know or who they have been introduced to through their networks.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Corporate law requires the board of directors to treat all shareholders equally under equal circumstances. Hence, valid reasons are required in order to allow for a selective information policy. Against the background that shareholders have no fiduciary duties towards the company, the board will rarely have valid reasons to selectively disclose confidential information to an activist shareholder within a proxy fight ahead of a shareholders' meeting.

The board is not obliged to disclose its engagement with activist shareholders for as long as no agreement is entered into. In the event that, for example, an activist shareholder requests that an agenda item be tabled at the next shareholders' meeting or that an extraordinary shareholders' meeting be convened, the board must make an ad hoc publication. For SIX listed companies, any such announcement must be distributed to SIX Exchange Regulation, at least two widely used electronic information systems, two Swiss daily newspapers of national importance, the website of the company and any interested party requesting to be included in the electronic distribution list.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

As activist shareholders do not have access to the share register of the company, they may publish their intentions on their website or in the media (eg, with open letters to shareholders or by approaching significant shareholders).

Generally, companies are free to approach their shareholders (eg, by way of letters to shareholders, public statements or individual approaches). As soon as the activist approach is publicly known, the media play an important role in shaping shareholder opinion in the run up to a shareholders' meeting. The board usually engages with the key shareholders in order to gain their support, which may require that the board compromises on certain issues. This shareholder engagement by the board must occur within the limits of the law, in particular, the transparency rules and rules on equal treatment (see question 17).

The board will also engage with proxy advisers in order to gain their support (possibly in the form of a special situations report) and, if successful, to make the proxy advisers' recommendation public to underline the viability of the board's position with its shareholders.

BÄR & KARRER

Mariel Hoch
mariel.hoch@baerkarrer.ch

Brandschenkestrasse 90
8027 Zurich
Switzerland
Tel: +41 58 261 50 00
Fax: +41 58 261 50 01
www.baerkarrer.ch

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

The shareholders' register of a Swiss company is not publicly available and the shareholders may therefore not receive a list of the registered shareholders from the company. In addition, Swiss companies are not obliged to distribute information prepared by a requesting shareholder to the other shareholders.

However, any shareholder holding at least 3 per cent in a listed company has to disclose, inter alia, the number of shares represented and the legal and beneficial owner. This information is available on the website of the respective stock exchange (eg, of the SIX Swiss Exchange). To foreign investors, it may come as a surprise that they are, as shareholders, not entitled to address their concerns with other shareholders by directly or indirectly using the company's share register or by including them in the company's proxy materials.

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

Activist engagement has become an established element of the Swiss capital market and is unlikely to disappear in the foreseeable future. After a few years of increased shareholder activism, many Swiss companies are aware of the related challenges and prepare for them, for example, by having their advisers lined up. Not all activist approaches are publicly known and not all published campaigns culminate in a proxy fight.

Some activists try to differentiate themselves from their competitors by stressing that they have a less short-term approach or that they wish to engage privately with the board of directors rather than in public campaigns. Swiss media are often divided in their assessment of the activists' requests and so is public opinion.

United Kingdom

Harry Coghill and Richard Burrows*
Macfarlanes LLP

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

Shareholder activism and engagement is governed by a range of UK and EU legislation. Some of the primary sources include:

- the Companies Act 2006 (the Companies Act);
- the Listing Rules;
- the Disclosure Guidance and Transparency Rules (DTRs);
- the EU Market Abuse Regulation (MAR);
- the City Code on Takeovers and Mergers (the Takeover Code); and
- the UK Corporate Governance Code (the UKCG Code).

The Companies Act is an Act of Parliament and applies to all UK incorporated companies. It is a key source of law for shareholders engaging in an activist campaign. For example, a shareholder holding at least 5 per cent of a company's issued share capital has the ability to requisition a general meeting of a company (s.303), or request specific resolutions to be tabled at a company's annual general meeting (s.338).

Both the Listing Rules and the DTRs are made and enforced by the Financial Conduct Authority (FCA). The Listing Rules apply to companies with a listing on the Official List, and prescribe the specific requirements that must be met to be eligible for listing, the admission and application process, and the continuing obligations to which listed issuers are subject. The DTRs seek to ensure there is adequate transparency of, and access to information in, UK financial markets and Chapter 5 (Vote Holder and Issuer Notification Rules) is often of particular interest to activist shareholders.

MAR is an EU regulation with direct effect in the United Kingdom. Like the Listing Rules and DTRs, it is also enforced by the FCA.

The Takeover Code contains rules made by the Takeover Panel under the Companies Act. It has been developed to reflect the collective opinion of those professionally involved in the field of takeovers as to appropriate business standards and as to how fairness to target shareholders and an orderly framework for takeovers can be achieved. It applies to companies incorporated in the United Kingdom, Channel Islands or Isle of Man that either: (i) have any of their securities admitted to trading on a regulated market or multilateral trading facility (eg, AIM) in those jurisdictions; and (ii) are public companies (or certain types of private companies) incorporated in, and with their central place of management and control in, any of those jurisdictions.

The UKCG Code applies to all companies with a premium listing in the United Kingdom (regardless of whether they are incorporated in the United Kingdom or elsewhere). The UKCG Code is not a rigid set of rules and is based around a set of principles and supporting provisions. This regulatory approach is often referred to as 'comply or explain' and is a trademark of the corporate governance framework in the United Kingdom.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Shareholder activism has continued to become more prevalent in the United Kingdom – both in the frequency of campaigns and the publicity they attract. Once again, 2018 saw the United Kingdom stand out as the busiest European jurisdiction for activist investors, with 23 activist campaigns launched – an increase from 20 in 2017. US hedge funds and alternative investors have continued to spearhead this activity, with a weaker pound perhaps increasing the sense of opportunity for activism.

In the United Kingdom, changes in board room structure remain a principal feature of recent campaigns and activists have continued to gain board seats, influence live M&A situations and advocate for spin-offs. However, it is notable that activists are increasingly adopting long-term strategies, focusing on rising environmental, social and governance concerns and exposing diversity issues.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

In some quarters, a negative perception of shareholder activism may remain. Amongst the general public and retail shareholders, that perception is perhaps derived from the reputation of shareholder activism in the United States – which has traditionally been seen as adversarial, hostile and opportunistic. However, there is a growing appreciation for the benefits of shareholder activism and continued shareholder engagement is seen as a key facet of good corporate governance in the United Kingdom. This attitude has been reflected in regulatory policy statements – for example, the Takeover Panel published Practice Statement 26 to allay investor's concerns that collective shareholder action could trigger the Takeover Code's provisions on mandatory offers.

In the United Kingdom, no particular industry is more susceptible to activism than others. A weaker pound and continuing Brexit uncertainty seem to have generally made UK companies an attractive opportunity for foreign investors. Typically, poor stock performance, inefficient use of capital deployment, poor corporate governance and the uneven performance of a company's divisions are all factors that can increase a company's likelihood of being targeted by activists.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

As mentioned in question 2, activist shareholders in the United Kingdom have typically been composed of hedge funds and other alternative investors, many of whom are based in the United States. The goals of activist shareholders are increasingly becoming more varied – they can be financial, aimed at increasing value for shareholders, and non-financial changes, such as the adoption of environmentally or ethically favourable policies and reactions to diversity issues. Activists are also increasingly prepared to take long-term positions to achieve these goals. An interesting recent development has been the reaction of institutional investors to activist campaigns. In the public sphere, institutional investors have traditionally been neutral and reluctant to air their grievances about management or strategy. However, some have taken a more proactive stance in recent activist campaigns, increasingly taking to public forums to lend their support (or opposition) to activists.

This shift in attitude in institutional investors is reflective of how shareholder engagement is growing in importance. Activist shareholders often provide a useful channel for a wider group of investors to air their dissatisfaction when they feel their concerns are not being appropriately recognised by management.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

Shareholder activism tends to focus on a myriad of areas. Globally, in 2018, 33 per cent of activist campaigns were M&A driven, with a sale of the company being the most common M&A objective. In the United Kingdom, such activity has historically been driven by dissatisfaction with strategy and a desire to shake up board composition. Executive remuneration and corporate governance failings can also be hot topics – with institutional investors teaming up with activists to push through change.

In recent times, perceived poor performance with respect to the environment (lack of preparedness for climate change), corporate social responsibility and political lobbying have attracted the attention of activists. The introduction of 'say-on-pay' legislation has sharpened the focus on compensation practices, while significant media or analyst criticism about a regulatory action or problematic product launch can cause discomfort in the shareholder base.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

Activist shareholders may pursue a range of both legal and non-legal strategies to achieve their objectives. The legal framework for activist strategy has not changed to any significant degree in recent years but the use of the tools has evolved. Given the more collaborative approach to shareholder engagement in the United Kingdom, the starting point for activists is often private engagement with a company's board.

If private engagement is unsuccessful, under the Companies Act, an activist can request a copy of the company's shareholder register – allowing them to solicit support from other investors should they think collective action would be more effective. If they hold the requisite number of shares, activists could requisition a general meeting or request certain resolutions to be proposed at the company's the next AGM. The success of this strategy of course depends on the levels of support the activist has managed to solicit from other large shareholders. However, it is important to remember that, for many resolutions, only a majority of those shareholders present and voting at the meeting is required so a low level of turnout can be helpful.

Activists can also show their dissatisfaction by voting against resolutions proposed by the company – for example, voting against directors' remuneration (which is voted on annually at each AGM), the remuneration policy (which must be voted on at least every three years) or even the re-election of the directors themselves. Activists can intervene in M&A situations to block a takeover, both by threatening to vote against a deal or by simply expressing their views on the takeover in public.

Lastly, activists will often turn to public announcements, websites and social media to reinforce their campaigns, particularly if they feel a company is ignoring them. The benefits of such tactics are obvious but the risk of falling foul of regulations such as MAR and the Takeover Code mean activists considering such a strategy must tread carefully.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

The starting point for the processes and guidelines for shareholders' proposals is the Companies Act. Under the Companies Act, certain actions by a company require shareholder approval. In giving that approval, shareholders may pass two types of resolutions: ordinary resolutions (which are passed by a simple majority) and special resolutions (which are passed by a 75 per cent majority). As referred to in question 6, these thresholds are calculated on the basis of those shareholders present (either in person or by proxy) at the general meeting – meaning that the number of votes may be a small percentage of the overall shareholder base. Ordinary resolutions are more common than special resolutions, which are reserved for more serious matters such as amending a company's constitution.

One of the ways under the Companies Act by which shareholders who hold at least five per cent of the paid-up share capital which carries voting rights may propose a resolution is by requiring the company to call a general meeting (section 303). Such a request may be in hard copy or electronic form and must be authenticated by the person or persons making it. It is usual to address the request to the directors of the company. The request should be sent in accordance with the Companies Act's requirements for communications to the company and care should be taken to check for any applicable provisions of the company's articles of association. In practice, such requests are normally sent in hard copy form and by a method that enables tracking of receipt. The Courts have held that any communication that members send seeking support for their proposal should give a fair, candid and reasonable explanation to members and should not be misleading. If a valid requisition request is made, the general meeting must be called within 21 days, the meeting itself must be held not more than 28 days after the date of the notice of the meeting and the company must bear the cost of convening the meeting.

Alternatively, shareholders may wish to propose a resolution to be voted on at the next AGM (section 338). The resolution must be one that may properly be moved, and is intended to be moved at that meeting. Resolutions that may not be properly moved at an AGM are those that, if passed, would be ineffective or those that are defamatory, frivolous or vexatious. The right to requisition a resolution under s.338 is open to those shareholders representing at least five per cent of the total voting rights or at least 100 shareholders holding the right to vote and who hold shares in the company on which there has been paid up an average sum, per member, of at least £100. Shareholders must ensure that the resolution is received by the company not later than six weeks before the AGM or, if later, circulation of the AGM notice. Unlike requests to convene general meetings, where shareholders wish to circulate a

resolution under section 338 they must bear the cost of doing so (other than where they have submitted their requisition notice before the end of the immediately preceding financial year). In doing so, they must deposit with, or tender to, the company a sum reasonably sufficient to meet the company's expenses of circulating the resolution.

In addition, shareholders can require the company to circulate a statement to shareholders in relation to any matter to be dealt with at a general meeting. The statement is limited to 1,000 words and the company must send it to every shareholder entitled to receive notice of the meeting.

In extreme cases, an activist shareholder may decide to exercise its right under the Companies Act to take legal action against the company, such as bringing a derivative claim in the name of the company against its directors or an unfair prejudice petition. These claims are discussed in more detail in question 10 but remain quite rare in the United Kingdom in relation to listed companies.

8 | May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

Shareholders have the ability to nominate directors to the board by either requisitioning a resolution to be proposed at the company's next AGM or by requisitioning a general meeting, as described in question 7.

If the shareholders wish to requisition a general meeting, the cost of convening the general meeting is borne by the company. Alternatively, subject to limited exceptions, shareholders who requisition the company to circulate a resolution to be proposed at an AGM must cover the company's costs of doing so.

9 | May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Shareholders have the ability to call a shareholders' meeting, using the process described in question 7.

In the United Kingdom, there is no statutory mechanism for shareholders of a public listed company to pass written resolutions in lieu of a meeting. However, a document signed by all shareholders of a public company may not be wholly ineffective. The Courts have held that where all shareholders, who would have a right to attend and vote on a matter at a general meeting of the company, unanimously assent to that matter by signing a written resolution, then an insistence on adhering to the prescribed procedural formalities for making the decision is not always necessary.

Notwithstanding that, public listed companies that want to pass written resolutions would encounter some obvious practical difficulties. It would be difficult to secure the individual written consent of each shareholder if there are a large numbers of shareholders. In addition, taking certain decisions by unanimous consent would appear to be inconsistent with provisions of the Company Law Codification Directive, which require a number of resolutions relating to the maintenance and alteration of capital to be taken by a public company in general meeting. The constraints contained in the Directive were the reason given for not extending the statutory written resolution procedure under the Companies Act to public companies.

Litigation

10 | What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

There are various types of litigation that a shareholder may initiate against a company or its directors. Some common examples include:

- a personal claim designed to uphold the 'statutory contract' created by the company's articles or to activate certain rights given to members under the Companies Act;
- an unfair prejudice petition under section 994 of the Companies Act by which a member might seek to contend that the company's affairs have been conducted in a manner that is unfairly prejudicial to the interests of the member or membership that includes the member – such claims generally seek a personal remedy for the benefit of the petitioner, commonly in the form of a share purchase order;
- a winding up petition under section 122(1)(g) of the Insolvency Act 1986, the 'just and equitable ground', under which a member may, in certain scenarios, be able to secure an order for the winding up of the company and the distribution of its assets in the ensuing liquidation; and
- a derivative claim (whether under statute, or in limited circumstances, common law) that provides a mechanism by which a member may seek to secure a remedy for and on behalf of the company itself.

Derivative claims are said to be derivative in that they derive from rights belonging to the company, and if successful, provide only an indirect benefit to members as shareholders in the company. Statutory derivative claims may be brought for negligence, default, breach of duty or breach of trust by a director, a third party or both. The claim may be brought by a member of the company and the expression 'member' has been extended beyond its normal meaning in company law for the purposes of statutory derivative claims. It includes not only the registered holder of shares but also a person to whom shares in the company have been transferred, or transmitted by operation of law, but who has not been registered as a member of the company. Outside of claims in the Competition Appeal Tribunal, class actions on behalf of shareholders are not as common in the United Kingdom as they are in the United States.

In terms of obtaining information, any person may inspect a company's register of members. A member of the company may inspect the register for free, but any other person must pay a prescribed fee. Additionally, any person may request a copy of the register of members, but must pay a prescribed fee, regardless of whether they are a member or not. As discussed in question 26, members can request (either for inspection or by providing copies of entries) a register of interests in the company's shares that have been disclosed to the company. Certain documents (such a company's articles of association) must be filed with the registrar of companies, and these documents are easily accessible on the Companies House website. Should a member wish to commence proceedings against the company, certain information will have to be disclosed as part of the disclosure process, to the extent that it is not legally privileged.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 | Do shareholder activists owe fiduciary duties to the company?

In the United Kingdom, shareholder activists owe no fiduciary duties to the target company.

Notwithstanding the absence of any fiduciary duty, there have been increased efforts in the United Kingdom to promote effective shareholder engagement, such as the development of the FRC's UK Stewardship Code (the Stewardship Code), establishment of the Investor Forum and the publication of best practice guidelines by bodies such as the Pensions and Lifetime Savings Association. The Stewardship Code applies on a 'comply or explain' basis and a revised version is scheduled to be published in the summer of 2019.

Compensation

12 | May directors accept compensation from shareholders who appoint them?

It is possible for directors to be employed by a shareholder and receive compensation from them but it would be unusual for directors not to be compensated directly by the company for their services. Director compensation will be determined by the company's remuneration committee in line with the remuneration policy. The levels of director compensation can be a contentious issue for shareholders, especially when they are afforded the chance to approve the remuneration policy at a company's AGM. It is normal for executive directors to be remunerated in line with the terms of their service contract with the company, while non-executive directors will be compensated as per the terms of their appointment letter.

If directors do receive payment from shareholders who appoint them, the arrangements would be likely to raise questions about conflicts of interest under the Companies Act, and such a director would still have to be re-elected annually at the company's AGM in line with the UKCG Code.

Mandatory bids

13 | Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

For the purposes of the Takeover Code, persons are deemed to be acting in concert when, pursuant to an agreement or understanding (whether formal or informal), they co-operate to obtain or consolidate control of, or to frustrate the successful outcome of, an offer for a company that is subject to the Takeover Code. The Takeover Code lists nine categories of person who will be presumed to be acting in concert with one another. These include a company, its parent, subsidiaries and their associated companies, and a company with its directors (together with their close relatives and the related trusts of any of them). These presumptions may be rebutted, following consultation with the Takeover Panel.

A mandatory bid is required to be made under Rule 9 of the Takeover Code where: (i) shareholders and any person acting in concert with them acquire shares carrying 30 per cent or more of the voting rights of a target company; or (ii) if a shareholder, together with its concert parties, holding not less than 30 per cent but not more than 50 per cent of the voting rights increases its holding. Rule 9 requires a mandatory offer to be made in cash or be accompanied by a cash alternative.

Following concerns in the market that the concert party provisions and mandatory bid rules in the Takeover Code were acting as a barrier to collective shareholder action, the Takeover Panel published helpful guidance for activists in the form of Practice Statement 26 (Shareholder activism). This confirmed that relevant provisions of the Takeover Code were not intended to constrain collective shareholder action.

According to the Practice Statement, shareholders will be subject to the Takeover Code's mandatory bid requirements when:

- those shareholders requisition a general meeting to consider a 'board control-seeking' proposal or threaten to do so; and
- after an agreement or understanding is reached between the shareholders that a board control-seeking resolution should be proposed or threatened, those shareholders acquire interests in shares such that the shares in which they are interested together carry 30 per cent or more of the voting rights in the company (or, if they are already interested in shares carrying 30 per cent or more of such voting rights, they acquire further interests in shares).

This means that even if a board control-seeking proposal were to be proposed by a group of shareholders, no mandatory bid obligation would be triggered if, at the time that any such agreement or understanding on the matter is reached, the shareholders do not hold the requisite number of shares.

Disclosure rules

14 | Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

There are certain circumstances in which a shareholder must disclose the level of its shareholding. Under DTR 5, a person must notify the issuer of the percentage of voting rights they hold as a shareholder (or holds or is deemed to hold through his or her direct or indirect holding of financial instruments) if, as a result of an acquisition or disposal of shares or financial instruments, the percentage of those voting rights exceeds or falls below the following thresholds:

- in the case of UK issuers, 3 per cent and each whole percentage threshold above 3 per cent; and
- in the case of non-UK issuers, 5, 10, 15, 20, 25, 30, 50 and 75 per cent.

In relation to UK issuers, the deadline for making the notification is within two trading days of the acquisition or disposal. For non-UK issuers, the deadline is within four trading days. In each case, the company must then disclose the notification to the market. Certain types of shareholder (primarily in the investment manager sector) are only required to make a disclosure under DTR 5 when they exceed or fall below the 5 per cent threshold of a UK issuer.

Under the Takeover Code, a person interested in 1 per cent or more of the securities of any relevant party to the offer must make an Opening Position Disclosure after the commencement of the offer period or an announcement is made that first identifies a non-cash bidder. An Opening Position Disclosure must be made within 10 business days. Subsequently, such a person must make a Dealing Disclosure if they deal in securities of any relevant party to the offer by not later than 3.30pm on the business day following the date of the dealing.

There is no requirement under UK law for any disclosure by a shareholder of its intentions in respect of its shareholding.

15 | Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

Holding derivative instruments can give rise to disclosure requirements under the DTRs. Under DTR 5.3, a person must make a disclosure notification in respect of any financial instrument that gives them a long economic position in respect of the company's shares. Many derivative instruments track the price of an underlying share exactly and simply pass through the economics to the derivative holder – meaning such instruments fall within the disclosure requirements of the DTRs. In calculating the thresholds referred to in question 14, both shares and financial instruments are counted for the purpose of establishing the relevant threshold.

In making an Opening Position Disclosure or Dealing Disclosure (as referred to in question 14), the question of whether someone is

'interested' in the securities of an offer party is widely defined and covers both options and derivative positions. Under the Takeover Code, the person making the disclosure may also have to include details of their concert parties' interests.

The Financial Services and Markets Act 2000 (Short Selling) Regulations 2012 were introduced in the United Kingdom to implement the EU Regulation on Short Selling. Under these regulations, a person must publicly disclose details of any net short position it has in relation to relevant shares:

- when the position reaches 0.5 per cent of the issued share capital of the company (the Initial Public Disclosure Threshold);
- at each additional 0.1 per cent above the Initial Public Disclosure Threshold (a Subsequent Public Disclosure Threshold); and
- when the position decreases below either the Initial Public Disclosure Threshold or a Subsequent Public Disclosure Threshold.

This disclosure must be made by 3.30pm on the trading day following which the person reaches, falls below or passes through the relevant Initial Public Disclosure Threshold or Subsequent Public Disclosure Threshold, as applicable.

Insider trading

16 | Do insider trading rules apply to activist activity?

Depending on the nature of the activist activity, insider trading rules may apply. It is important that activists are aware of the possible implications their actions may have under the market abuse and insider dealing regimes.

Activist activity will often entail private communications with a company's board. In the course of those communications, it is possible that inside information about the company could be divulged to the activist. Under MAR, inside information is defined as information that is:

- of a precise nature;
- has not been made public;
- relates, directly or indirectly, to one or more issuers, or to one or more financial instruments themselves; and
- if made public, would be likely to have a significant effect on the price of those financial instruments, or related derivative instruments.

Once the activist possesses inside information, should they use it to deal in financial instruments to which the information relates, they would commit an insider dealing offence under MAR. It is possible that the activist's strategy itself constitutes inside information. The position under MAR and the FCA's general approach, however, is that it may not be abusive to the market if the activist is simply carrying out investments on the basis of their own knowledge and resources. However, it is clear that activists should be cautious in these situations.

If an activist discloses inside information to another person, other than in the proper course of the exercise of his or her employment, profession or other duties, that would constitute an unlawful disclosure of inside information under MAR. However, it is not just the activist themselves who should be concerned. If another shareholder engaged in dealing on the basis of their knowledge of the activist's intentions and strategy, that could be deemed to be market abuse. In general, all shareholders should be mindful to ensure that they do not make any comments that give rise to false or misleading signals about financial instruments, as this can constitute market manipulation under MAR.

There is a level of overlap between the civil regime of MAR and the criminal regime under the Criminal Justice Act 1993. The FCA has discretion to pursue a criminal prosecution or take civil action in respect of the same behaviour.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

Directors are under no different standard of duty when considering an activist proposal than when they are making any other board decision.

Directors' fiduciary duties are derived from equity and have been codified in the Companies Act. They include the duty to:

- act within their powers;
- promote the success of the company;
- exercise independent judgement;
- avoid conflicts of interest;
- not accept benefits from third parties; and
- declare an interest in a proposed transaction or arrangement.

Directors owe the same fiduciary duties to the company regardless of whether they are also a shareholder, or have been appointed by a shareholder. In contrast, activists acting solely in their capacity as shareholders owe no fiduciary duties to the company.

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

Shareholder activism continues to grow in prevalence in the United Kingdom so effective shareholder engagement is becoming an even more important issue in the boardroom. Just as the nature of activist campaigns has evolved, so too have the tactics of boards in response to those campaigns. The key change in recent times is the increasing willingness of companies to be proactive and engage with shareholders on the issues they raise.

Companies can adopt a variety of strategies in preparation for an activist campaign. As a matter of best practice, companies should monitor their register of members regularly and maintain an open dialogue with shareholders. It is important that companies undergo self-evaluation exercises to identify areas to strengthen and to mitigate potential vulnerabilities – getting ahead of investor concerns. Companies should have a plan in place for how to react to an activist campaign that includes dealing not only with the activist but also other external stakeholders. Finally, companies would be well advised to take a less reactive posture to an activist attack and seek opportunities to control the narrative, increase leverage with key shareholders and understand investor views beyond the activist.

Defences

19 | What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Any company can be the target of shareholder activism and, outside of good governance and continued shareholder engagement, companies do not have many defences to avoid being the subject of an activist campaign. Structural or 'poison pill' defences do not feature in the United Kingdom. Indeed, invoking such a defence could constitute a breach of a director's fiduciary duties to the company. Activists typically focus on companies that are experiencing (or are perceived to be experiencing) financial underperformance, so financial outperformance relative to its peers is one of the best defences available to a company.

In respect of a takeover offer for a public company governed by the Takeover Code, the target directors must abide by certain rules. One of the key principles of the Takeover Code is that the target board must not deny shareholders the opportunity to decide on the merits of the offer. As part of that principle, they must obtain shareholder approval for any act that may result in any offer or bona fide possible offer being frustrated. As discussed in question 18, the most effective way in which companies can combat shareholder activism is proactive shareholder engagement.

Proxy votes

20 Do companies receive daily or periodic reports of proxy votes during the voting period?

Companies can elect to receive updates on proxy votes as often as they like during the voting period. The proxy totals will normally be confidential and often will only be communicated to key individuals at the company and its advisers. Disclosing proxy numbers improperly could constitute a market abuse offence under MAR, as described in question 16.

Settlements

21 Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

The use of private settlement agreements to end activist disputes is becoming increasingly popular in the United Kingdom, just as the nature of activist campaigns has continued to evolve. Settlement agreements provide a means to avoid the significant drain on resources that a protracted public proxy battle may entail. Typically, such agreements will include an agreed set of actions to be taken by the company, such as the appointment of the activists' nominee(s) to the board. In return, there may be a standstill agreement in relation to the activist's shareholding in the company. One notable example in the United Kingdom was the settlement agreement entered into between Elliott Management and Alliance Trust. Under the terms of that agreement, Alliance Trust undertook to appoint two non-executive directors, nominated by Elliott. In return, Elliott agreed to support the board on all other resolutions and not to agitate publicly against the company until after its next AGM.

As discussed in question 4, institutional investors in the United Kingdom are becoming much more proactive with regard to activist campaigns than they would traditionally have been. As a result of this heightened engagement, investors are increasingly aware (and vocal) about the dangers of a company settling with an activist too soon. It is sometimes the case that the short-term, event-driven strategies of some activists is at odds with the more long-term focused investment horizon of the typical institutional investor.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

Once considered a perfunctory matter, shareholder engagement is now a key facet of good corporate governance in the United Kingdom and companies are alive to its importance. This has been driven, in part, by the development of best practice guidance. For instance, the Investor Forum, which was established in October 2014, aims to position stewardship at the heart of investment decision-making by facilitating dialogue, creating long-term solutions and enhancing value for UK listed companies and investors alike. Similarly, in 2017, ICSA and the Investment Association published guidance on how company boards should engage with their key stakeholders when making strategic decisions.

Of course, not all shareholders are alike. The topics on which they want to engage and their appetite for doing so will vary depending on the level of their investment, their particular resources and interests and other reasons. Typically, institutional investors invest on a long-term basis and so they often prefer to drive organic change rather than seeking shorter-term changes. As noted in question 4, private engagement efforts are often initiated by the investor, reflecting the more collaborative approach to shareholder activism in the United Kingdom.

23 Are directors commonly involved in shareholder engagement efforts?

It is not unusual for directors to be involved in shareholder engagement efforts. Shareholders are not homogenous, a fact to which boards are sensitive and they will tailor their engagement practices accordingly. Large institutional shareholders will almost always demand engagement with board members. Retail shareholders are less likely to meet with directors outside of the company's AGM. As a matter of best practice, it is recommended that all directors are involved in shareholder engagement efforts, a principle that has been codified in the UKCG Code.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Although there is no legal obligation to do so, as a matter of good corporate governance, companies should ensure that there are effective measures in place to facilitate direct communication between shareholders and the board. It is normal for companies to disclose details of such communications in their annual reports.

When companies are making disclosures to shareholders, they must be careful not to breach the rules surrounding inside information and market abuse. Listed companies are obliged to disclose to the market inside information that a reasonable investor would use when making investment decisions. Such disclosures must be made as soon as possible and are typically done through a Regulatory Information Service (RIS). In certain circumstances, these disclosures can be delayed: where an immediate disclosure would likely prejudice the issuer's legitimate interests; delay of disclosure is not likely to mislead the public; and the issuer is able to ensure the confidentiality of the information.

Inside information may be disclosed selectively when the person to whom the information is being disclosed owes the company a duty of confidentiality to the company and needs the information for proper reasons. MAR requires companies to keep up-to-date insider lists of persons who have access to information. As discussed in question 16, it is an offence for a person to trade on the basis of inside information.

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

Where an activist is seeking to obtain support from other shareholders, they should be mindful of the market abuse regime. The communication could constitute inside information if it disseminates non-public, price-sensitive information. Under MAR, the scope of what can amount

to inside information includes information about a third party's trading strategy. Accordingly, activists may choose to publish details about their plans at the outset of their campaign, perhaps by way of an open letter. In these circumstances, the activist must be careful to not make false or misleading statements.

Due to a greater emphasis on shareholder engagement in the United Kingdom, companies will often have private conversations with their major shareholders. Quite often, large institutional investors may hold positions in both the company and the activist. In such circumstances, it is important that the investor has appropriate internal safeguards to control the receipt of any inside information appropriately.

The Companies Act contains provisions to allow a public company to investigate who has an interest in its share capital by issuing a section 793 notice to any person whom it knows, or has a reasonable cause to believe, to be interested in its shares or to have been so interested at any time in the preceding three years. The notice may require the recipient to state whether it has an interest in the company's shares and to give details of those holdings. Public companies will typically use an RIS announcement to communicate directly with its shareholders.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

Under the Companies Act, shareholders can request to inspect or receive a copy of the company's register of members. They are entitled to inspect the register without charge – when a copy is requested, shareholders must pay the prescribed fee. If the company wants to resist the request (either to provide a copy of the register or to allow a member to inspect it), it must apply to Court and demonstrate that the request has not been made for a 'proper purpose'. There is no statutory definition of what constitutes a 'proper purpose'. The Institute of Chartered Secretaries and Administrators has published a non-binding, non-exhaustive list of examples and the Courts have held that the phrase should be given its ordinary, natural meaning.

The register of members will only display the legal owners of the shares. However, shareholders also have the ability to request (either for inspection or by providing copies of entries) a register of interests in the company's shares that have been disclosed to the company. Such disclosures will have been made when the company issued a section 793 notice, as referred to in question 25. As with its register of members, the company may only resist a request with regards to its register of interests if that request has not been made for a proper purpose.

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

2018 was another record year for shareholder activism in the United Kingdom. Activists have continued to demand board seats, drive M&A activity and exert pressure over perceived corporate governance failings. Elliott Advisors, the most prolific activist investor worldwide, led campaigns that prompted the UK retailer Whitbread to offload Costa Coffee, while it also backed Melrose's hostile takeover of GKN. Sherborne's attempt to have its founder, Edward Bramson, appointed to the board of directors of Barclays in order to implement change at Barclays' investment bank has gathered much media attention recently.

MACFARLANES

Harry Coghill
harry.coghill@macfarlanes.com

Richard Burrows
richard.burrows@macfarlanes.com

20 Cursitor Street
London
EC4A 1LT
United Kingdom
Tel: +44 20 7831 9222
www.macfarlanes.com

This campaign has been notable given the size of the target company – and signifies that activists are not afraid to invest in large companies in highly regulated industries.

It is also noteworthy that the objectives behind activist campaigns have continued to diversify. This has been influenced by recent regulatory developments that have sharpened activists' attention on environmental, social and governance issues. For example, the Dutch activist Follow This launched high-profile campaigns at Royal Dutch Shell and BP, putting pressure on both companies to cut their emission targets in line with the Paris Agreement. Shell subsequently announced that it would set firm short-term targets to reduce carbon emissions and link these to pay from 2020.

Given the rise of shareholder activism, the importance of effective shareholder engagement has never been more pronounced. However, 2018 saw some high-profile examples of what can happen when sufficient engagement has not taken place. In October, Unilever scrapped plans to forgo its dual Anglo-Dutch market listing and to consolidate its headquarters in Rotterdam. The move was defeated when large institutional investors expressed objections to the plan. Columbia Threadneedle, a top 10 investor in the company, later criticised Unilever for a lack of engagement and failing to convince UK shareholders of the merits of the move. This public criticism is in itself noteworthy, as large institutional investors in UK companies are traditionally reluctant to criticise management in public.

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United States

Adam Emmerich, Trevor Norwitz, Steven Cohen, Sabastian Niles and Jenny Lin
Wachtell, Lipton, Rosen & Katz

GENERAL

Primary sources

1 What are the primary sources of laws and regulations relating to shareholder activism and engagement? Who makes and enforces them?

In the United States, corporations are subject to a dual legislative regime, being governed by both state corporation laws and federal securities and other laws. In addition, publicly traded companies must comply with the listing rules of the exchange on which they are listed. Beyond laws and regulations, there are best practices and guidelines advocated by proxy advisory firms, institutional investors and others in the investment community that touch on shareholder activism and engagement issues.

State law

Each corporation is incorporated in the state of its choosing. State corporation law establishes the fiduciary duties, powers and authority of directors of both privately held and publicly traded companies, as well as rights and powers of the companies' shareholders. More than half of all public companies in the United States are formed in Delaware. A small state that has 'specialised' in the area of business law, Delaware has developed a highly sophisticated judiciary, a very deep body of case law relating to corporate matters, and a legislature that is both experienced in matters of corporation law and highly responsive when changes are needed. Most of the other states follow to a greater or lesser degree the Model Business Corporation Act (which differs from Delaware law in some specific respects although the two regimes are quite similar in the way they deal with most issues), but Delaware is generally viewed as having a major influence on the corporate law of other states. For that reason, Delaware General Corporate Law (DGCL) will serve as a reference point in this chapter. The enforcement of state corporation laws, including the decisions made by boards of directors, generally falls on the companies' shareholders in the form of direct or derivative litigation, on behalf of the company, against its officers and directors for non-compliance with state law.

Federal law

Federal laws most directly related to shareholder activism and engagement are laws governing securities trading, include the Securities Act of 1933 (the Securities Act), the Securities Exchange Act of 1934 (the Exchange Act), the Public Company Accounting Reform and Investor Protection Act of 2002 (the Sarbanes-Oxley Act) and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the Dodd-Frank Act) and the regulations that have been promulgated by the federal agencies under all of these acts. The enforcement of these laws and regulations are the purview of the Securities and Exchange Commission (SEC). For example, shareholder activists are required to comply with beneficial ownership reporting requirements under section 13 of the Exchange Act, which generally require a person or 'group' who has acquired direct or indirect beneficial ownership of more than 5 per cent of an outstanding class of equity securities to file a report with certain information with SEC within 10 calendar days of crossing the 5 per cent threshold and promptly after material changes in their position or intentions. Companies must navigate the disclosure requirements of the Exchange Act in reporting on corporate governance matters in their periodic disclosure and their annual meeting proxy statement disclosures.

Federal laws relating to protecting competition can also impact activism. In particular, the Hart- Scott-Rodino Antitrust Improvements Act (the HSR Act) requires anyone acquiring securities in the United States to file a form and wait for clearance (generally 30 days although this can be accelerated) before crossing specified dollar thresholds. Because the lowest threshold is currently around US$90 million, this filing may be the first time a company learns that an activist is accumulating a position in its stock (although activists are often able to avoid filing under the HSR Act while building their position by buying through separate funds).

Informal standard setters

Alongside the above regulatory regimes, public companies also have to be cognisant of the proxy advisory firms, primarily Institutional Shareholder Services (ISS) and Glass Lewis, which advise institutional investors how they should vote and whose recommendations in contested situations can often be outcome determinative. These proxy advisors publish guidelines for governance 'best practices' and which issue voting recommendations and reports that, while not having the force of law, are very influential with voters and so have to be taken into account.

There are no rules mandating engagement with shareholders but companies do engage with their significant institutional shareholders on a regular basis both during the annual 'proxy season' when companies may be seeking shareholder support, and 'off-season' in order to maintain good relations and understand issues that shareholders may care about. In any engagement with shareholders or other outside parties, companies must comply with Regulation FD, which prohibits a company from selectively disclosing material non-public information.

Shareholder activism

2 How frequent are activist campaigns in your jurisdiction and what are the chances of success?

Shareholder activism and engagement is increasingly viewed as a fixture in the governance of publicly traded companies. Every proxy season sees many activist campaigns of all kinds ranging from high-profile economic campaigns involving large public companies and 'name-brand' activists to lower profile efforts by social activists seeking to advance some social, political or governance agenda using the

corporate voting machinery. In discussing shareholder activism in the United States, it is helpful to separate shareholder activists into two separate categories:

- 'economic' activism by hedge funds or other 'fund' activists: this category consists of professional investors who make sizeable (but still minority) investments in a target company and then publicly or privately advocate for change, often characterised by a drive for near-term shareholder value; and
- 14a-8 activism, by which shareholders submit proposals under Exchange Act Rule 14a-8, which requires a company to include a shareholder proposal in its proxy materials if certain requirements are met (for example, the shareholder owns the lesser of US$2,000 or 1 per cent of the securities entitled to vote on the proposal for at least one calendar year prior to submission of the proposal). 14a-8 proponents vary widely and include retail shareholders, social justice groups, religious organisations, labour pension funds, individual gadflies and other coalitions.

In recent years, both types of activism are on the rise. Assets under management by activist hedge funds remain at elevated levels, encouraging continued attacks, including on many large successful companies. Meanwhile, environmental, social and governance (ESG) concerns have given rise to an increasing number of campaigns by 14a-8 activists, both individuals and institutional shareholders.

In calendar year 2018, there were a record number of 226 companies targeted by 247 activist campaigns, leading to a record number of 161 board seats claimed by activists. The vast majority of these resulted from settlements between the company and the activist rather than an actual vote in a contested election. Even though a number of high-profile activists have had a challenging year from a performance perspective, activist funds and shareholders are expected to continue to be a major force going forward.

Many public companies receive one or more shareholder proposals under Rule 14a-8 every one or two years relating to governance or other ESG issues. In the 2018 proxy season, 788 shareholder proposals were filed. Most of these are 'precatory' proposals, not seeking to directly implement a change but requesting the board to take a specified action. The success of these depends very much on the particular topic (for example, a request to eliminate a staggered board would almost invariably receive a very high level of support, while a request for a company to study gender pay disparities will depend on whether investors perceive there is a problem and how the company has responded). Because the proxy advisory firms have policies to recommend against directors standing for re-election if they do not implement the will of the shareholders as expressed in a shareholder resolution, companies are increasingly responsive to shareholder proposals that receive broad shareholder support.

3 How is shareholder activism generally viewed in your jurisdiction by the legislature, regulators, institutional and retail shareholders and the general public? Are some industries more or less prone to shareholder activism? Why?

The merits of shareholder activism remain a hotly debated subject in the United States. In general, corporate America and its supporters view much activist activity as short-term oriented, often greed-driven and abusive, and detrimental to the ability of companies to plan and execute long-term strategies. The institutional shareholder community, supported by many in the sell-side analyst community, the press and academia, consider shareholder activism a valuable mechanism for holding boards of directors to account. Institutional shareholders have been on either sides of activist fund attacks. While some recognise the damage an activist attack may have on the long-term value of a company, others are working with activist funds, either behind the scenes or co-sponsoring an attack. There is a general recognition that some shareholder activism can be constructive (typically characterised by open-minded behind-the-scenes engagement), while other forms of activism, where there is less quiet engagement and more aggressive public mudslinging, is often destructive. Activists benefit in the public eye by claiming and being accorded credit for changes that take place in companies after they announce their involvement. In some cases, this is deserved; in others, the improvements were not attributable to (and sometimes were even despite) the activist's involvement, but companies are happy to let the activist take credit as long as they move on and attack someone else. Activist funds do best (indeed some studies suggest that they only produce above-market returns) when they succeed in getting their target company sold. In those cases, it often appears that their involvement 'unlocked value', but this is often a dubious proposition as it compares a known result against the unknown. In short, the perception of shareholder activism is still in flux. It is only in the last few years, with the widescale elimination of staggered boards and other takeover defences, that decision-making power has shifted out of the boardroom to the institutional shareholder community, and that community (including passive investors such as index funds and influential proxy advisors such as ISS and Glass Lewis) is still trying to understand how to use its newfound power.

Legislators and regulators have largely stayed out of the fray of shareholder activism. The SEC has sought to play an evenhanded role ensuring that both sides provide full and fair disclosure and are not misleading in their proxy solicitations. Even when prompted (and encouraged by the legislature in the Dodd-Frank Act) to curb abuses by activists of the Regulation 13D early-warning disclosure system, the SEC has declined to act but preferred to maintain the current 'balance of power'. The frequency and impact of hedge fund activism has prompted some legislators to propose federal legislation (such as the Brokaw Bill and Senator Elizabeth Warren's attempt to achieve stakeholder corporate governance by way of mandatory federal incorporation), but to date these changes have not received significant support.

Meanwhile, 14a-8 activists have been looked upon more favourably by institutional shareholders as a way to achieve certain ESG goals, such as board diversity and environmental sustainability. For example, the recent proxy access campaign (pushing companies to adopt provisions in their governing documents that would allow certain long-term shareholders the right to include their director nominations on the company's proxy card) has garnered the support of institutional shareholders such as the California State Teachers' Retirement System (CalSTRS) as a way to improve corporate governance where the regulators have failed to act.

Activism in the United States is broadly spread across industries, although naturally some individual activists gravitate towards certain industries once they feel they have established a good understanding of the industry. In 2018, the technology, industrials, consumer and financial institutions industries continued to have the highest aggregate value of activist fund positions. Certainly no industry is immune from shareholder activism. Companies in highly regulated industries, such as banks and insurance companies, were once seen as less likely targets for an activist campaign. Although this may still be true, the targeting of AIG (by Carl Icahn) and the Bank of New York Mellon (by Nelson Peltz) makes it clear that even companies in highly regulated industries can be subject to fund activism.

As for 14a-8 activism, certain industries are more susceptible than others, given the ESG focus of some campaigns. For example, the New York City Comptroller and the New York City Pension Funds' initial Boardroom Accountability Project, a campaign for proxy access, specifically targeted carbon-intensive energy companies, among others, as a

way to improve governance at companies that were seen to be 'most vulnerable to long-term business risks related to climate change'.

4 What are the typical characteristics of shareholder activists in your jurisdiction?

As noted above, in the United States it is important to distinguish between the two main types of activists, economically-driven activist hedge funds (which threaten and wage full-blown proxy fights) and social and political activists (who rely mostly on submitting shareholder proposals using SEC Rule 14a-8). The former group (activist hedge funds) are typically headed by charismatic, ambitious and aggressive individuals. Their funds are typically structured to provide the fund managers with a 20 per cent 'carried interest' on any upside in their portfolio, providing a significant incentive to lock-in short-term gains on their positions. The latter group (14a-8 proponents) vary widely and include all varieties of retail shareholders, social justice groups, religious organisations, pension funds, trade unions, individual gadflies and other coalitions with shared interests.

In addition, in recent years, traditional institutional investors have become involved in the activist arena as well. Historically, such institutional holders were passive money managers, generally voting with the board's recommendation and selling their shares if they lost faith in the company. In recent years, however, traditional investors have worked alongside activist investors, sometimes actively soliciting their involvement in situations, and sometimes openly cosponsoring activist campaigns. Certain institutions have even mounted their own campaigns against their portfolio companies through the submission of 14a-8 proposals, such as the New York City Pension Fund and its Boardroom Accountability Project.

5 What are the main operational governance and sociopolitical areas that shareholder activism focuses on? Do any factors tend to attract shareholder activist attention?

Shareholder activists have focused on a wide variety of capital structure changes, such as increasing leverage, stock splits, dividends and repurchases, and strategic changes, such as a company sale or breakup or other operational changes, including changes to management and boards of directors. In 2018, strategic changes and mergers and acquisitions transactions were featured prominently in the various campaigns. While calls for company sales remain prevalent, activists have begun to make more sophisticated demands, such as the breakup of conglomerates (eg, UTC) and reorganisation of complex corporate structures (eg, Procter & Gamble).

Often, shareholder activist campaigns will couple a call for capital structure changes and strategic changes with criticism of and suggested changes to corporate governance (eg, eliminating structural defences, board refreshment, management changes, criticism of executive compensation and other governance changes). A significant percentage of the activist campaigns in 2018 included a demand for board seats at the target company. In the United States, 63 per cent of completed campaigns resulted in at least one board seat for the activist, adding up to a total of 199 board seats won by activists.

ESG issues are also areas of focus, especially for institutional investors. BlackRock, in its CEO's annual letter, noted that 'every company must not only deliver financial performance, but also show how it makes a positive contribution to society'. In the 2018 proxy season, social and environmental proposals make up 43 per cent of all proposals submitted. There has been heightened activism around climate change, particularly in the context of the late-2015 Paris Climate Accord and the latest administration's deregulatory stance, including calls for more expansive environmental and sustainability disclosure, with growing focus on sustainability measurement and accountability. There has also been a continued focus on lobbying and political-spending disclosure by target companies following the 2016 presidential election. Board diversity has also been in the spotlight, receiving expressions of support from notable institutional investors such as State Street and Vanguard. After recent tragedies in the United States, selected institutional investors are pushing companies for stronger positions on gun control. Conventional activist funds have also embraced this development, by launching separate funds with social and environmental goals or including ESG factors in their overall investment process.

SHAREHOLDER ACTIVIST STRATEGIES

Strategies

6 What common strategies do activist shareholders use to pursue their objectives?

The strategies employed by activist investors vary depending on the intended goal. Key tactics include:

- Deal activism – either by pushing for a merger, sale or divestiture transaction by the target company or after announcement of such a transaction, exercising shareholder rights to appraisal in hopes of getting a higher price, encouraging a topping bid by a third party, trying to influence the combined company or the integration process or trying to scuttle the deal.
- Operational activism – advocating for cost-cutting measures, strategy change, portfolio review or management turnover, in each case, often in combination with a proposal to replace the CEO and/or members of the board of directors.
- Financial engineering or balance sheet activism – demanding a target company undergo a capital structure change in the form of buying back shares, declaring a special dividend, or overhauling the company's tax planning.
- ESG activism – advocating for environmental, social and governance change, including eroding a company's takeover defences to facilitate economic activism goals.
- 'Short' activism – accumulating a short position and combining it with negative public campaigns, white paper publications, among others.

These more conventional tactics are often coupled with more innovative approaches, such as economic arrangements among funds, partnering with a hostile third-party bidder, calling special meetings for 'referendums' and combining traditional proxy fights with 'vote no' campaigns. Some activists have looked to the courts in their campaigns by using litigation to extend director nomination deadlines or to challenge the target company's decision in proxy fights. Activists have also been known to employ new methods to engage retail shareholders, including using social media and redoubling engagement efforts with institutional shareholders and proxy advisers.

Processes and guidelines

7 What are the general processes and guidelines for shareholders' proposals?

A shareholder may propose that certain business be brought before a meeting of shareholders by providing notice and complying with applicable provisions of state law and the company's by-laws and charter. The company's 'advance notice' by-laws will generally set forth the time requirements for delivering the proposal (for example, that the proposal be received by the company's corporate secretary not more than 90 days and not less than 60 days before the meeting), other procedural requirements (such as a description of the ownership and voting interests of the proposing party) and limitations on the types of

proposals that can be submitted (for example, that a proposal may not be submitted that is substantially the same as a proposal already to be voted on at the meeting). It is often costly to submit a proposal in this manner because the soliciting shareholder must develop its own proxy materials and conduct its own proxy solicitation. However, serious fund activists seeking to effect a change in the company's strategy or to nominate directors do proceed in this manner under the by-laws of the company rather than relying on Rule 14a-8.

Under Exchange Act Rule 14a-8, a shareholder may submit a proposal to be included in the company's proxy statement alongside management's proposals (avoiding the expense of developing independent proxy materials and conducting an independent proxy solicitation). Rule 14a-8 sets forth eligibility and procedural requirements, including:

- that the proposing shareholder has continuously held, for at least one year by the date the proposal is submitted to the company, the lesser of US$2,000 in market value or 1 per cent of the company's securities entitled to vote on the proposal and continue to hold those securities through the meeting date;
- that the proposal be no longer than 500 words; and
- that the proposal be received at least 120 calendar days prior to the anniversary of the date of release of the company's proxy statement for the previous year's annual meeting.

If the shareholder has complied with the procedural requirements of Rule 14a-8, then the company may only exclude the proposal if it falls within one of the 13 substantive bases for exclusion under Rule 14a-8 (eg, that the proposal would be improper under state law, relates to the redress of a personal claim or grievance, deals with a matter relating to the company's ordinary business operations, relates to director elections, has already been substantially implemented, is duplicative of another proposal that will be included in the company's proxy materials or relates to a specific amount of cash or stock dividends). A company will often seek 'no action relief' from the SEC staff to exclude a shareholder proposal from the company's proxy materials on one of the bases of exclusion listed above. If 'no action relief' is not granted, a company could, but rarely does, seek a declaratory judgment from a court that the shareholder proposal may be excluded from the company's proxy statement.

Shareholder 14a-8 proposals are often precatory or non-binding, and do not require implementation even if the proposal receives majority support. Shareholder proposals may, however, be binding if the proposal is with respect to an action reserved for the shareholders (for example, a proposal to amend the by-laws may be binding depending on state law and the company's by-laws).

In recent years, even precatory proposals have become an effective way for shareholders to compel change, because ISS and Glass Lewis will generally recommend that shareholders vote against directors who do not promptly implement the expressed will of the shareholders.

8 May shareholders nominate directors for election to the board and use the company's proxy or shareholder circular infrastructure, at the company's expense, to do so?

The right of shareholders to nominate candidates for election as director is considered a fundamental element of corporate democracy. That right, and the process to be followed to exercise it, is typically contained in a company's by-laws. Companies are not, however, required by state or federal law to permit shareholders to use the company's proxy infrastructure, at the company's expense, to nominate directors for election to the board. For many years, there were efforts by shareholder activist groups to require companies to give shareholders access to the company's proxy statement to nominate their candidates. This culminated in the adoption by the SEC of Exchange Act Rule 14a-11, which would have granted proxy access (limited to 25 per cent of the board) to 3 per cent shareholders who have held their shares for at least three years. However, this rule was struck down by the federal courts in 2011.

Proxy access was thrust back onto the agenda in large part through Rule 14a-8 proposals by individual shareholders, as well as large institutional investors, like the New York Pension Funds. In reaction to the popularity of these proxy access proposals, most large public companies have since adopted proxy access by-laws with standards similar to proposed Rule 14a-11. At the time of writing, approximately 67 per cent of the S&P 500 have adopted a proxy access by-law with most allowing nominations for 20 per cent of the board seats by a shareholder or group of shareholders (up to 20 shareholders) that have held 3 per cent or more of the company's shares for three years or more. Given the relative infancy of proxy access by-laws and the percentage and holding period to be met, we have not yet seen many instances of shareholders utilising this new option to nominate directors, but these nominations may become more popular in the future.

9 May shareholders call a special shareholders' meeting? What are the requirements? May shareholders act by written consent in lieu of a meeting?

Whether a shareholder may call a special meeting depends on the corporate laws of its state of incorporation and its organisational documents. With respect to Delaware corporations, under DGCL section 211(d), a company's certificate of incorporation or by-laws may authorise shareholders to call a special shareholder meeting. The certificate of incorporation or by-laws would then set forth the procedural requirements for calling a special meeting, including the minimum holding requirements for a shareholder to call a special meeting. At the time of writing, about two-thirds of companies in the S&P 500 do provide for this right in their organisational documents, while a third do not. For those companies that do allow shareholders to call special meetings, the required ownership threshold varies considerably, from as low as 10 per cent to as high as 50 per cent, although 25 per cent is sometimes cited as the most common threshold.

The institutional shareholder groups, and the proxy advisers ISS and Glass Lewis who make voting recommendations to them, generally favour providing shareholders with the right to call a special meeting. In 2018, there was a significant increase in the number of proposals to lower the ownership percentage required to call special meetings (typically from around 25 per cent to as low as 10 per cent, which is the level preferred by ISS and Glass Lewis), but most of these proposals were unsuccessful as most major institutions believe that 20 per cent or 25 per cent is the right level.

Whether shareholders may act by written consent without a meeting also depends on state corporate law and the particular company's organisational documents. With respect to Delaware corporations, under DGCL, section 228, shareholders may act by written consent in lieu of a shareholders' meeting, unless the company's charter provides otherwise. At the time of writing, 70 per cent of S&P 500 companies do not allow their shareholders to act by written consent without a meeting. While ISS and Glass Lewis state that they consider the right to act by written consent an important shareholder right, most large institutions appreciate that, as long as shareholders have the right to call a special meeting if necessary, action by written consent is unnecessary, as well as being potentially destabilising and undemocratic (in that it disenfranchises minority shareholders).

Litigation

10 What are the main types of litigation shareholders in your jurisdiction may initiate against corporations and directors? May shareholders bring derivative actions on behalf of the corporation or class actions on behalf of all shareholders? Are there methods of obtaining access to company information?

Shareholders may initiate two main types of litigation against a corporation and its directors – derivative and direct, depending on the nature and sufferer of the alleged harm. A company's shareholder can also initiate proceedings against a company to inspect certain corporate books and records of the company.

Shareholders may bring derivative actions on behalf of a corporation where there has been an alleged breach of the directors' or officers' fiduciary duty of care, fiduciary duty of loyalty or other wrongdoing. The purpose of a derivative suit is to remedy harm done to the corporation usually by directors and officers. Derivative suits face a number of procedural hurdles, which depend in large part on the jurisdiction in which they are brought. Certain states require that, before a derivative lawsuit is filed, the shareholder make a 'demand' on the board of directors to bring the lawsuit on the corporation's behalf. The demand requirement implements the basic principle of corporate governance that the decisions of a corporation – including the decision to initiate litigation – should be made by the board of directors. If a shareholder makes such a demand, the board of directors may consider whether to form a special litigation committee of independent directors to evaluate the demand. If the board of directors refuses the demand, the shareholder may litigate whether the demand was 'wrongfully refused'. Certain jurisdictions recognise an exception to the demand requirement where demand would be 'futile'– namely, if a majority of the board of directors is conflicted or participated in the alleged wrongdoing. In such circumstances, it might be appropriate and permissible for the shareholder to skip the demand process and proceed directly to filing a complaint (in which he, she or it would need to demonstrate that a demand would have been futile).

While shareholder derivative suits are brought for the benefit of the corporation, shareholder direct and class actions address unique, direct harms to the particular shareholder plaintiffs. In the M&A context, it has become common for shareholders to initiate class actions against target companies and their boards of directors, alleging that the target company's board violated its fiduciary duties by conducting a flawed sale process that did not maximise value for the companies' shareholders. In such instances, a critical factor in determining the outcome of the litigation will be which standard of review is applicable to the board's conduct; in other words, the deferential 'business judgement rule' or a heightened standard of review that some jurisdictions have adopted (such as Revlon, Unocal or 'entire fairness'). Many public companies have adopted 'exculpation' provisions in their governance documents, which provide that directors cannot be personally liable for damages arising out of breaches of the duty of care. However, a director generally cannot be indemnified or exculpated for breaches of the duty of loyalty, including the obligation to act in good faith.

Aside from derivative suits and direct actions, a Delaware company's shareholders also have the right, under DGCL section 220, to inspect certain books and records of the company; provided that they have 'proper purpose' for seeking such materials. Under DGCL section 220, to be eligible for the inspection right, a shareholder must establish both a 'proper purpose' for the inspection – namely, one that is reasonably related to the person's interest as a shareholder, and that the scope of the books and records sought is no broader than what is 'necessary and essential to accomplish the stated, proper purpose'. To exercise this right, a shareholder should first make a 'demand' on the company. If the company or an officer of the company refuses the demand or does not respond within five business days, the shareholder may apply to the court for an order to compel the inspection.

SHAREHOLDERS' DUTIES

Fiduciary duties

11 Do shareholder activists owe fiduciary duties to the company?

A majority or significant shareholder may owe fiduciary duties to other shareholders if it exercises control. Such fiduciary duties are generally relevant in the context of a self-dealing transaction (where the controlling shareholder is effectively on both sides of the transaction). This set of facts is not normally present in a shareholder activist campaign.

Of course, if an activist succeeds in having directors elected to a company's board, those directors owe the same fiduciary duties to the company and its shareholders as any other directors. The courts have recognised (most explicitly in the recent Delaware case *In Re PLX Shareholders Litigation*) that shareholder activists often have different interests and focus more on the short term than the company's shareholders in general but directors designated by (or even employed by) activists owe their fiduciary duties to the company and shareholders as a whole.

Compensation

12 May directors accept compensation from shareholders who appoint them?

It is not illegal for directors to receive compensation from shareholders who appoint them. This often happens, for example, when employees of an activist hedge fund are themselves nominated and elected as directors. However, it would be important to analyse whether acceptance of compensation from a nominating shareholder might be contrary to the directors' fiduciary duties. Under federal securities laws, the compensation would also likely have to be disclosed. In addition, the corporation itself may have limitations in its by-laws or charter with respect to directors accepting direct compensation from shareholders who nominate them. It is common practice for companies to require a director candidate to sign an agreement that includes a representation by the nominee that he or she is and will not become party to any undisclosed agreement with any person other than the company with respect to compensation in connection with his or her service as a director of the company.

It is important to distinguish between compensation paid to a nominee prior to nomination and ongoing compensation paid to a director after the director is on the board. It is not uncommon for an activist to offer some modest compensation to candidates in exchange for agreeing to stand for election in a proxy contest. The argument is that such payments may be necessary to recruit high-quality independent candidates to participate in a proxy contest, and that as long as these arrangements are disclosed, they should not create significant conflicts. Some activists have attempted to go further and offer compensation to their candidates after election that could influence the manner in which they act as directors (eg, by giving them an incentive to sell the company quickly). Attempts to adopt by-laws to outlaw these types of 'golden leash' arrangements were rejected by ISS and some institutional shareholders. However, the general recognition in the corporate governance community that compensation arrangements of this type raise serious questions regarding alignment of economic incentives and can create serious conflicts of interest have led to them being extremely rare.

Mandatory bids

13 Are shareholders acting in concert subject to any mandatory bid requirements in your jurisdiction? When are shareholders deemed to be acting in concert?

There is no 'mandatory bid' requirement under US federal tender offer rules or Delaware corporate law.

We note for completeness that at least three states have statutory 'control share cash-out' provisions (of which, in some cases, companies may opt out), providing that if a bidder gains voting power of a certain percentage of shares (20 per cent in Pennsylvania, 25 per cent in Maine and 50 per cent in South Dakota), other shareholders can demand that the controlling shareholder purchase their shares at a 'fair price' (effectively providing the equivalent of dissenters' rights applicable to the acquiror rather than the issuer).

Shareholders acting in concert (the US terminology is acting 'as a group') do however have disclosure obligations under section 13 of the Exchange Act, as described below. Shareholders may be deemed to have formed a 'group' when they agree to act together in connection with acquiring, holding, voting or disposing of a company's securities.

Disclosure rules

14 Must shareholders disclose significant shareholdings? If so, when? Must such disclosure include the shareholder's intentions?

Accumulations of large blocks of equity securities trigger reporting obligations under section 13 of the Exchange Act, which requires any person or group that acquires beneficial ownership of more than 5 per cent of a class of a public company's registered voting equity securities to file a beneficial ownership report with the SEC disclosing its ownership and certain other information. For this purpose, 'beneficial ownership' generally means direct or indirect voting or dispositive power over a security, including through any contract, arrangement, understanding, relationship or otherwise. Disclosure obligations may also be triggered by membership in a 'group' that beneficially owns more than 5 per cent of a class of equity securities of a public company, as discussed below. Acquisition or ownership of a class of non-voting securities does not trigger any filing obligations for these purposes.

Generally, an individual investor or group that beneficially owns more than 5 per cent of a class of equity securities of a public company must report its holdings on Schedule 13D within 10 days of its holding exceeding 5 per cent, unless it is eligible to report its holdings on a short-form Schedule 13G. Importantly, a Schedule 13D requires detailed disclosures regarding the filer's control persons, source of funds and the purpose of the acquisition of the securities, including any plans for further acquisitions or intention to influence or cause changes in the management or business of the issuer. Material changes in the previously reported facts require 'prompt' amendment of a Schedule 13D. The securities laws do not define what 'promptly' means, but it depends on the materiality of the information to be disclosed.

Certain investors can satisfy their section 13 beneficial ownership reporting obligations by filing the simpler and less detailed Schedule 13G. These generally include specified institutional investors (eg, banks, broker-dealers, investment companies and registered investment advisers) acting in the ordinary course and without a control purpose or effect, and passive investors acting without a control purpose or effect. There are also other exceptions that may allow an investor to report beneficial ownership on a Schedule 13G instead of a Schedule 13D.

As 'beneficial ownership' is based on the power to vote or dispose of a security, whether ownership of a significant derivative position in the equity securities of a public company will trigger a Schedule 13D or Schedule 13G filing requirement depends on the type of the particular derivative. Cash-settled derivatives generally do not give rise to beneficial ownership because they do not create a contractual right to acquire voting or dispositive power, but other types of derivatives may constitute beneficial ownership of the underlying securities.

In addition, section 16(a) of the Exchange Act requires a person or group to disclose when their beneficial ownership of a company's equity securities exceeds 10 per cent. At that point, and as long as they remain 10 per cent holders, such persons are generally deemed to be insiders subject to section 16(b)'s short-swing profit disgorgement rules. Various exceptions apply; for example, section 16 is not applicable to the securities of foreign private issuers, and institutional investors can generally disregard shares held on behalf of clients or in fiduciary accounts when determining section 16 beneficial ownership.

The HSR Act may also impose a filing obligation with the Federal Trade Commission and the Department of Justice on certain investors. For 2018, an investor's acquisition of a company's voting securities or assets is reportable if the transaction value exceeds US$90 million (this dollar amount is adjusted annually). Once the reporting threshold is reached, there is also a 30-day waiting period that is imposed, during which the transaction cannot close. These filings are not public but either party may choose to make the fact of the filing public. In addition, if either party requests and is granted early termination of the waiting period, the fact of the grant of early termination will be made public. Finally, there are certain structures that can be used (involving put-call options or the use of multiple funds as acquisition vehicles) that may effectively allow an investor to accumulate the right to stock well in excess of the HSR Act threshold. Counsel should be consulted regarding the use of such methods as the rules are highly technical.

15 Do the disclosure requirements apply to derivative instruments, acting in concert or short positions?

For the purposes of section 13, a person is also deemed to be the beneficial owner of securities over which the person can acquire voting or dispositive power within 60 days (provided that, where any such rights to acquire securities are acquired with a control purpose or effect, beneficial ownership is triggered, regardless of whether the rights are exercisable within the 60-day time frame). Thus, an option, warrant, right or conversion privilege that results in voting or dispositive power and that can be exercised within 60 days creates current beneficial ownership.

An investor may generally talk with other investors and management about its investment in a company without tripping any disclosure requirements under the securities laws. However, if the investors coordinate activities or agree to act together with other investors in connection with acquiring, holding, voting or disposing of the company's securities, the investors may be deemed to have formed a 'group' for purposes of sections 13 and 16 of the Exchange Act. An investor group will have its holdings aggregated for purposes of determining whether the relevant reporting thresholds have been crossed. For example, if three investors, each with beneficial ownership of 2 per cent of a company's voting shares, form a group, they will have to file a Schedule 13D (or Schedule 13G, if eligible) because their shares collectively exceed the 5 per cent threshold.

As currently drafted, the Exchange Act does not require the disclosure of short positions, even large ones. In 2010, the Dodd-Frank Act amended section 13(f) of the Exchange Act to direct the SEC to prescribe rules for the public disclosure of certain details with regard to short sales that, at a minimum, would occur every month. However, the SEC has yet to implement these provisions and adopt a disclosure regime for short positions.

Insider trading

16 | Do insider trading rules apply to activist activity?

The SEC's insider trading rules prohibit a person from buying or selling a security, in breach of a fiduciary duty or other duty of confidence, while in possession of material non-public information about that security. The rules also prohibit the 'tipping' by insiders of such material non-public information and the trading by the recipient of such information. Insiders typically include a company's directors, officers, employees, counsels, significant shareholders and any other person that has a duty not to trade on material non-public information. Additionally, most, if not all, companies have adopted insider trading policies that apply to directors, officers, employees, controlling shareholders and their respective affiliates in order to minimise the likelihood of insider trading.

An activist may come into possession of material non-public information in its capacity as a significant shareholder or an affiliate of a director, where it has nominated a director onto the company board. In such a situation, the activist would be subject to the SEC's insider trading rules, as well as any insider trading policies implemented by the company. In order to preserve their trading flexibility, many activists prefer not to have their own insiders on the board.

COMPANY RESPONSE STRATEGIES

Fiduciary duties

17 | What are the fiduciary duties of directors in the context of an activist proposal? Is there a different standard for considering an activist proposal compared to other board decisions?

The fiduciary duties of directors are governed by state corporation law. Directors have basic fiduciary duties of loyalty (not putting their own interests above those of the company) and due care. Directors' decisions are typically reviewed under the default standard of the 'business judgment rule', which is a presumption, absent evidence to the contrary, that disinterested and independent directors acted on an informed basis and in the honest belief that the action taken was in the best interest of the company. As such, board decisions are not easily overturned. When a company receives an activist proposal, the same principles apply and the board must review and consider the proposal to determine whether it is in the best interest of the company and its shareholders.

In Delaware, in certain instances, a board's action in response to an activist proposal may be subject to an enhanced level of judicial scrutiny. If the board adopts defensive measures after a takeover or similar proposal is launched or threatened, the decision may be reviewed under the heightened Unocal standard, under which the directors must show both that reasonable grounds for believing there to be a danger to corporate policy and effectiveness and that the defensive measure was reasonably proportional in relation to the threat. Generally, the board has wide latitude to take defensive measures within a range of reasonableness, so long as such measures are not coercive or preclusive. Actions that impede the shareholder franchise (for example, if an activist is seeking to replace a majority of the directors and the board increases the board size to deny the activist a majority) are liable to be overturned by the courts (under the *Blasius* line of cases).

Preparation

18 | What advice do you give companies to prepare for shareholder activism? Is shareholder activism and engagement a matter of heightened concern in the boardroom?

Our advice is always situation-specific; that being said, principles for responding to activists include:

- Everything should go through the CEO (or, if applicable, chair of the board) – all executives and directors should refer activist and takeover approaches, overtures and conversations to the CEO. It is essential that the company speak with one voice. The CEO should keep the board of directors informed and solicit director input for decisions and reactions. Activists may try to contact directors directly, in which case, directors should keep in mind that all conversations are 'on the record' and any comments may be used by the activist in their proxy and press materials.
- Maintaining board unity is essential – a unified, supportive board is essential to producing the best outcome, whether the goal is resisting an activist agenda or negotiating the best possible settlement. It is critical to avoid having an activist drive a wedge between management and the board. Honest and open debate should be encouraged, but kept within the boardroom.
- Except in 'clear conflict' situations, special committees with additional financial and legal advisers are not advisable – special committees usually hinder board unity, overemphasise the role of advisers, deprive directors of the most valuable source of information and do not enhance directors' legal protection in non-conflict situations. 'Clear conflict' means the involvement of interested directors or senior management being on the other side of the transaction.
- Act and speak as though everything you do and say will be made public – appreciate that the public dialogue is often asymmetrical; while activists can, often without consequence, make personal attacks and use aggressive language, the company cannot respond in this manner. Any sign of discouragement, self-criticism of performance or execution or sign of dissension in the boardroom will be used against the company.
- The board has time and flexibility in responding and plenty of legal latitude – with respect to activism, the board has no special duty to implement an activist's proposals. The board's general fiduciary duties apply to decisions made in contemplation of or in reaction to shareholder activism. When considering an activist's proposals and criticisms, it is the board's responsibility to make decisions in the best interests of the company and stockholders.
- Remain focused on the business – activists and takeover approaches can be distracting and time-consuming for a board and management, but continued strong performance of the business, though not an absolute defence, is one of the best defences.

Defences

19 | What defences are available to companies to avoid being the target of shareholder activism or respond to shareholder activism?

Structural defences

Many of the structural defences that, under state law and a company's charter and by-laws, may be available to companies to resist a hostile takeover bid can also improve the company's ability to resist an activist attack. However, in recent years, most large corporations have given up many of their defences. For example, if a company has a staggered board, an activist can only win a minority of the board seats in any one election cycle. If a company does not have a staggered board, an activist can propose to take control of the board (and we are

increasingly seeing efforts to do so). Whereas most S&P 500 companies had a staggered board 15 years ago, about 90 per cent today do not. Because a staggered board has to be provided for in the company's charter, companies that have given up their staggered board are unable to implement one now.

Other provisions of a company's corporate profile that implicate its vulnerability to an activist attack are whether shareholders can call a special meeting, or act by written consent, which determine whether the company is only vulnerable at its annual meeting or throughout the year.

Most companies have adopted by-laws providing for advance notice and other requirements for shareholder proposals and director nominations, that provide some advance warning of an attack. If a company's charter permits shareholders to act by written consent, the board cannot eliminate that danger but can implement a by-law requiring a shareholder who wants to act by written consent to ask for a record date, in a process that can also provide a few weeks of notice of a consent solicitation.

The board can still implement a shareholder rights plan (also known as a 'poison pill') to prevent an activist or group of activists acting in concert from acquiring stock in the company above a specified threshold, but that level is typically set at 15 or 20 per cent and activists generally do not need to go that high to have an effective attacking platform. Some states also have anti-takeover statutes that may discourage hostile acquirers or activists going over a specified threshold of ownership. For example, Delaware (along with several other states) has a 'moratorium' anti-takeover statute that restricts a shareholder that has acquired 15 per cent or more (but less than 85 per cent in the same transaction) of the company's outstanding shares, without approval of the board, from engaging in certain business combination transactions with the company for a period of three years.

The effectiveness of the available structural defences will vary depending on the situation. There are no defences that make a company immune to shareholder activism. Sometimes the very existence of one or more of these defences can actually create a vulnerability in an activist situation because the proxy advisory firms and major institutions dislike structural defences such as staggered boards and will support an activist to protest what they consider imperfect governance.

Other defences

Aside from traditional structural defences, the best defensive measures that a company can take (aside from keeping its stock price high) is to maintain active outreach and engagement with the company's core, long-term shareholders. Understanding investor concerns and maintaining an ongoing dialogue can not only identify potential areas of vulnerability for the company but also help boards in avoiding public shareholder activist campaigns and securing shareholder support if faced with one. Additionally, companies and boards should continually monitor corporate governance benchmarks and trends and compare the company's corporate governance practices to evolving best practices to stay abreast of hot topic issues and address any potential vulnerabilities.

Proxy votes

20 | Do companies receive daily or periodic reports of proxy votes during the voting period?

During a contested situation, it is not unusual for companies to receive frequent updates on proxy vote tallies. Even in uncontested situations, for relatively routine annual shareholder meetings, companies will often choose to receive periodically updated reports on proxy voting (if for no other reason than to confirm that they will have a quorum).

Historically, Broadridge, which is the single largest agent collecting vote tallies, would provide the vote tallies both to the shareholder proponent and the company. However, in May 2013, after certain brokers objected to the release of this information to shareholder proponents, Broadridge changed its policy to provide vote tallies to the shareholder proponent only if the company affirmatively consents. Proxy rules are currently silent on preliminary vote tallies despite calls by various interest groups for SEC rulemaking on the subject. We would also note that some companies have received Rule 14a-8 shareholder proposals regarding vote tallies – namely keeping the interim vote tallies confidential, even from the company, in certain situations. Depending on the language of the specific proposal, it may be possible to exclude the proposal on 'ordinary business' grounds. Of the shareholder proposals that have gone to a vote, none received majority support; however, certain institutional investors, such as Vanguard, have indicated support for confidential voting. Certain companies have responded by adopting a policy on interim vote tallies, allowing Broadridge to provide non-public interim tallies to qualifying shareholders in certain situations.

Settlements

21 | Is it common for companies in your jurisdiction to enter into a private settlement with activists? If so, what types of arrangements are typically agreed?

It is not uncommon for companies to enter into settlements with activists in order to end proxy fights and activist campaigns. Depending on the form of the settlement, the terms are sometimes publicly disclosed or filed by the company. The type and terms of the arrangement vary depending on the activist's demands. Typically, the agitating activist will receive a number of board seats as part of the settlement. Starboard Value led the way in 2018, winning 29 board seats exclusively through settlements with target companies (out of a total of 161 board seats won by activists last year). In campaigns where the activist has demands or proposals other than seating new directors, the settlement will usually involve the implementation of one or more of the activist's demands, either in its entirety or tailored in some way to be more acceptable or feasible for the company, usually in addition to the appointment of certain activist-approved directors on the board.

SHAREHOLDER COMMUNICATION AND ENGAGEMENT

Shareholder engagement

22 | Is it common to have organised shareholder engagement efforts as a matter of course? What do outreach efforts typically entail?

Effective engagement with major shareholders is an essential element of activist defence. As shareholder activism has become more commonplace, most companies have shareholder outreach procedures in place to ensure constant, periodic dialogue with major shareholders. It is not unusual for companies to plan tours and participate in industry conferences as a way to meet shareholders and engage with them on issues and concerns they may have. The format of the shareholder outreach varies and includes published letters to shareholders, in-person meetings, teleconference calls and speaking engagements or panels at industry conferences. However, widely published, written communications are seen as impersonal and do not facilitate an exchange between the company and its shareholders. Thus, companies often rely on other engagement methods in addition to published communications.

23 Are directors commonly involved in shareholder engagement efforts?

The company's senior management typically leads shareholder engagement efforts but directors are typically involved as well. Today, boards of directors are expected to have a lead independent director or a non-executive chair of the board who can assist management in engaging with investors. By having directors involved, the company is in a better position to address shareholder concerns regarding corporate governance and other issues that affect the company's longer-term value. However, the involvement of a director, independent or otherwise, may not be helpful or appropriate in every situation. The company should consult with its board and advisers to determine when directors should be involved and prepare its director(s) adequately if it is decided that one or more directors should be part of the shareholder engagement effort.

Disclosure

24 Must companies disclose shareholder engagement efforts or how shareholders may communicate directly with the board? Must companies avoid selective or unequal disclosure? When companies disclose shareholder engagement efforts, what form does the disclosure take?

Generally speaking, companies are not required to publicly disclose their shareholder engagement efforts, although companies often choose to disclose such efforts in their annual meeting proxy to show responsiveness to shareholder concerns. Companies also often announce which industry conferences their directors and officers will be attending or any large-scale shareholder meetings the company will be hosting. Large companies often also publish transcripts of or otherwise make available recordings of speeches or comments made by directors and officers at industry conferences and such shareholder meetings on the companies' website. In their annual meeting proxy, companies are required to disclose how security holders may communicate with the board of directors.

In engaging with investors and others, companies should make sure to comply with Regulation FD, a rule intended to ensure that companies do not engage in selective or unequal disclosure. Regulation FD applies when a company or a person acting on the company's behalf (ie, all senior officers and any other officer, employee or agent of the company who regularly communicates with the financial community) discloses material non-public information to investors or security market professionals. If such disclosure is intentional (ie, the person communicating the information either knows, or is reckless in not knowing, that the information is both material and non-public), then to cure the violation the information must be disclosed simultaneously to the public. If such disclosure is inadvertent (ie, the person communicating the information did not know, and should not have known, that the information is both material and non-public), then the information must be disclosed to the public as soon as possible. Disclosures under Regulation FD often consist of furnishing the information on Form 8-K with the SEC or publication in other widely disseminated sources, including press releases.

Disclosures to persons who expressly agree (even orally) to maintain the disclosed information in confidence are expressly exempted from Regulation FD. For this reason, before discussing material non-public information with a shareholder, friend or foe, a company will often insist on signing a confidentiality agreement. We note for completeness that a shareholder may not want the company to disclose material non-public information to it, because the shareholder's ability to trade in the stock may then be limited (because of insider trading concerns).

Communication with shareholders

25 What are the primary rules relating to communications to obtain support from other shareholders? How do companies solicit votes from shareholders? Are there systems enabling the company to identify or facilitating direct communication with its shareholders?

The federal proxy rules are the primary rules relating to communications to solicit support from shareholders. Any statement that is designed to result in the giving or withholding of a proxy must be filed under the proxy rules, comply with certain legending and informational requirements, and not be misleading. In addition, companies that choose to hold private discussions with certain shareholders must be mindful of Regulation FD. Under Regulation FD, a company may not selectively disclose material non-public information to certain individuals or entities who may trade on that information or pass it on to others, without making public disclosure of that information simultaneously (or as soon as possible if inadvertent). Companies solicit formal votes from shareholders at both annual and special meetings, each of which is subject to federal proxy rules and certain notice requirements under the DGCL or a company's by-laws, or both. Shareholders may cast absentee ballots or designate a proxy to vote either at such proxy's discretion or with specific and binding guidance.

In the context of a proxy contest, each side will typically issue its own detailed proxy statement and also write one or more 'fight letters', or argumentative white papers or PowerPoint decks. All of these materials must be filed with the SEC under a proxy materials (14A) cover page.

The SEC staff has provided guidance on applying the proxy and tender offer rules when statements are made that constitute proxy solicitations through certain social media channels. The guidance permits the use of a hyperlink to information required by certain rules when a character-limited or text-limited social media channel, such as Twitter, is used for regulated communication.

Access to the share register

26 Must companies, generally or at a shareholder's request, provide a list of registered shareholders or a list of beneficial ownership, or submit to their shareholders information prepared by a requesting shareholder? How may this request be resisted?

Under Exchange Act Rule 14a-7, if a company has made or intends to make a proxy solicitation in connection with a shareholder meeting, the company must, upon written request of a shareholder entitled to vote at the meeting, either give the requesting shareholder the shareholder list or mail the requesting shareholder's soliciting materials to the company's shareholders at the requesting shareholder's expense. Most target companies choose the latter option, mailing all materials themselves.

In addition, state corporate law and a company's charter and by-laws may provide for access to shareholder lists under additional circumstances. For example, as described in question 10, Delaware corporate law allows shareholders to inspect the company's stock ledger and its other books and records so long as the shareholder submits a demand under oath and explains the 'proper purpose' of the request. The company may resist this demand by asserting, and proving in court if necessary, that the shareholder's inspection purpose is not one that is reasonably related to the person's interests as a shareholder of the company or that the scope of records requested is too broad for the shareholder's purposes. However, given Rule 14a-7, it may be hard for a company to argue that a shareholder list and ownership information is either not necessary for an activist shareholder's proxy solicitation or otherwise too broad for the solicitation purpose.

UPDATE AND TRENDS

Recent activist campaigns

27 Discuss any noteworthy recent, high-profile shareholder activist campaigns in your jurisdiction. What are the current hot topics in shareholder activism and engagement?

Activists set new records in 2018, targeting the largest number of companies (nearly 300), deploying more capital and winning a greater number of board seats (161) than ever before. Campaigns by the most well-known activist hedge funds are surging, and there are more than 100 hedge funds currently engaged in activism. Activist hedge funds have significantly more than US$100 billion of assets under management, and remain an 'asset class' that attracts investment from major traditional institutional investors. Although a number of institutional investors are beginning to question whether hedge fund activism should be supported or resisted, and will act independently of activists, the relationships between activists and more traditional investors in recent years have encouraged increasingly frequent and aggressive activist attacks. Several mutual funds and other institutional investors have on occasion also deployed the same kinds of tactics and campaigns as the dedicated activist funds.

The 2019 proxy season, already well underway as of the time of writing this chapter, has seen a significant increase in the number of control slates of director candidates being named. Historically, proposing a control slate to take over a majority of the board of directors has been viewed as a challenge for activists, because serious long-term investors, and those who advise them, are not quick to hand control of the board over to an unknown entity (even though their bar for adding a few new directors into the mix is much lower). In 2019, however, activists have been using the 'control slate' (or even proposals to replace the board entirely) as a weapon to try to negotiate a settlement giving them more board seats then they would have been able to negotiate had they nominated a 'short slate'. It remains to be seen whether this tactic will be successful and continue to be used.

In addition to the 'traditional' activist shareholder, 'debt default activism' is also on the rise. In these situations, debt investors purchase a company's debt on the theory that the company is already in default and then actively seek to enforce that default in a manner by which they stand to profit. The playbook of such an activist starts with the investor identifying a financing transaction, even one effected years earlier, that it can claim did not comply with a covenant in the issuer's debt documents. Next, the investor amasses both a short position in the company's debt (in some cases through a credit default swap that collects upon a default) and a long position in the debt sufficient to assert a default, and possibly even a blocking position (typically the activist's long exposure is smaller than their short position, so the investor is 'net short'). The investor, finally, asserts the alleged default, often in a public letter, and if its long position is large enough (usually 25 per cent of a bond tranche), it can also serve a formal default notice, triggering a high-stakes litigation. To cite a recent example, bondholders of Safeway have asserted defaults arising from the company's acquisition by Albertsons, first announced in 2014. Although analysts differ on the merits of the bondholders' claim, the nearly four-year gap between the closing of the Albertsons deal and the default allegations is remarkable.

WACHTELL, LIPTON, ROSEN & KATZ

Adam Emmerich
aoemmerich@wlrk.com

Trevor Norwitz
tsnorwitz@wlrk.com

Steven Cohen
sacohen@wlrk.com

Sabastian Niles
svniles@wlrk.com

Jenny Lin
jylin@wlrk.com

51 West 52nd Street
New York
New York 10029
United States
Tel: +1 212 403 1000
Fax: +1 212 403 2000
www.wlrk.com

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