

CORPORATE AND SECURITIES LAW

Alert

NEWS FOR THE CLIENTS AND FRIENDS OF BASS, BERRY & SIMS PLC

2008 Proxy Season Trends

August 13, 2008

With many public companies having held their 2008 annual shareholders' meeting, we are beginning to see some trends emerge that illustrate the increased prominence of activist shareholders in corporate governance. While it will be several months before a full sampling of results have been reported and analyzed, we wanted to highlight a few of the more notable developments.

Election Contests Brought By Activist Hedge Funds Often Being Settled

Rather than engaging in proxy contests with hedge fund dissidents, many companies are negotiating with the dissident shareholder and agreeing to provide board representation to avoid expensive and distracting contests. Activist hedge funds have obtained seats pursuant to settlement agreements at the New York Times Co., Zale Corporation, Charming Shoppes Inc., Silicon Storage Technology and Federal Signal Corporation, among other companies. The costs associated with waging a proxy battle against an insurgent hedge fund, the loss of management focus during the fight and the risk of a negative recommendation from RiskMetrics are among the factors cited by companies that have sought to settle proxy battles. In the settlement agreements, in addition to providing board representation to insurgent shareholders, companies are also agreeing to governance changes, such as declassification of staggered boards. In exchange for allowing board representation, the company frequently receives a standstill that prevents the activist hedge fund from engaging in takeover attempts or election contests through the next year's annual meeting, although the duration and other terms of the standstill vary.

"Vote No" Campaigns Continue to Provide Activists with Inexpensive, Effective Tactic

Activist shareholders continue to use "vote no" campaigns against incumbent board nominees. Since proxies are not solicited in these campaigns, shareholders do not have to comply with the SEC's proxy solicitation rules and are able to achieve desired results without incurring significant legal expenses. The shareholder also does not have to comply with any advance notice requirements in these contests, as the shareholder is not proposing a competing slate of directors or proposing additional business to be considered at the meeting. Campaigns usually rely on press releases and advertising, and may include mailings to shareholders through Broadridge (formerly ADP). In light of the increased adoption of majority vote requirements for elections of directors, "vote no" campaigns are a growing concern. Examples of recent "vote no" campaigns, with varying success, include Washington Mutual, Morgan Stanley, Ryland Group and Toll Brothers, companies that have been negatively impacted by the recent housing and credit market downturns.

Fewer Shareholder Proposals Coming to Vote

As activists seek to force corporate governance issues through shareholder proposals, companies are responding by constructively engaging in discussion with these shareholders and negotiating withdrawals of the proposals, while at the same time becoming more aggressive in seeking to exclude shareholder proposals from the company's proxy statement. For instance, early proxy season returns tracked by Deloitte's corporate governance group indicate that nearly half of pay-for-performance and majority voting proposals had been withdrawn by shareholders. Meanwhile, according to an initial sampling by RiskMetrics, the SEC has permitted companies to exclude more shareholder proposals brought under Rule 14a-8 during the 2008 proxy season when compared to the 2007 proxy season. The SEC allowed exclusion about 68 percent of the time, up from 48 percent last year. (The effect is magnified by the fact that companies have been challenging even more of the proposals submitted this year — 33 percent in 2008 versus 20 percent in 2007 — and there has been no indication by the SEC of a generally increased willingness to permit exclusion of shareholder proposals.) Grounds for exclusion under the rule include procedural defects and a number of substantive grounds, such as proposals that are materially false or misleading or that relate to personal grievances.

With respect to the issues raised by shareholder proposals, Deloitte notes that majority voting proposals continue to be an activist favorite. Additionally, proposals to repeal staggered boards have spiked and the shareholders' right to call special meetings has become a hot issue as well. In its early sampling, RiskMetrics noted that special meeting proposals were receiving support in excess of 50 percent on average.

E-Proxy Update

Broadridge recently released statistical information on electronic delivery of proxy materials through May 31, 2008. A total of 634 companies utilized the "Notice and Access" model of electronic proxy delivery through Broadridge during that time. Compared against 2007, those companies that used electronic delivery saw a drop in the average quorum per meeting of only about 2 percent of the number of shares outstanding. However, the percentage of retail shares that voted fell from approximately 34 percent on average in 2007 to approximately 16 percent on average among those companies using electronic delivery of proxy materials through May 31, 2008. Only about 1 percent of those shareholders that received a Notice of Internet Availability of Proxy Materials requested a full set of proxy materials. These statistics suggest that electronic delivery of proxy materials can provide savings in the form of decreased material and mailing costs with little effect on quorums. However, the significant decreases in retail voting with the use of electronic delivery of proxy materials should be considered in light of the composition of a company's shareholder base.

If you have any questions about this Corporate and Securities Law Alert, or would like any additional information, please contact any Bass, Berry & Sims attorney in the Corporate and Securities Practice Area.

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315 Deaderick Street • Suite 2700 • Nashville, TN 37238-3001 • (615) 742-6200
The Tower at Peabody Place • 100 Peabody Place, Suite 900 • Memphis, TN 38103-3672 • (901) 543-5900
1700 Riverview Tower • 900 S. Gay Street • Knoxville, TN 37902 • (865) 521-6200