Symbolic Corporate Governance Politics

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Abstract

How are we to understand the persistent gap between rhetoric and reality that characterizes so much of corporate governance politics? In this Article, we show that the rhetoric around a variety of high profile corporate governance controversies (including shareholder proposals asking boards to redeem poison pills, proxy access, majority voting in director elections, the remarkable absence of mandatory proposals, and shareholder proposals to remove supermajority voting requirements) cannot be justified by the material interests at stake. We then consider a variety of explanations including “public interest” analyses, “public choice” analyses, and the possibility that corporate governance politics, like politics more generally, has a substantial “symbolic” element. Returning to Thurman Arnold’s \textit{The Folklore of Capitalism}, we ask whether there is an analogous “Folklore of Corporate Governance” and, if so, what role the controversies over corporate governance reform play in reconciling the gap between our ideals and reality. We then consider some of the implications of this understanding of corporate governance politics.

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Symbolic Corporate Governance Politics

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Introduction

Poison pills. Proxy access. Separation of the Chair and CEO positions. Staggered boards. Majority voting. Secret ballots. Independent directors. Say on pay. How many battles have been fought over corporate governance reform? How much ink has been spilled over what the partisans present as burning issues? Each controversy has claimed to be important. Yet, in retrospect, or even from a contemporary disinterested perspective, the stakes hardly seem to justify the intensity of the contest. What could be going on?

This is hardly an unusual situation. The material stakes in political disputes are often unrelated to the vigor of those contests. Sometimes, even after high profile, bitterly fought battles over policy, nothing changes. Sometimes, the apparent winners of a contest end up worse off and the losers better off. How is this gap to be understood, especially when it is so common as to be predictable?

In this Article, we consider the possibility that corporate governance politics, like politics more generally, may have a significant “symbolic” element in which the stakes, and the intensity, are largely divorced from the specific issue being debated but instead serve a variety of different functions, including a “mythological” or “ritual” function. In Part I, we contrast the “symbolic” view of politics and law described in Thurman Arnold’s *Folklore of American Capitalism* and related analyses with more traditional “public interest” and “public choice” explanations. Then, in Part II, we review a selection of corporate governance controversies and show that they typically display a striking gap between rhetoric and reality. In Part III, we consider the extent to which the different perspectives can explain that gap. In Part IV, we

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consider the implications of the symbolic aspects of corporate governance politics. We close with a brief conclusion.

Part I: Politics as Folklore and Myth

Thurman Arnold was a fascinating character. Born in Wyoming in 1891, educated at Princeton and Harvard Law School, he started teaching law at the University of Wyoming in 1921, moved to the college of law at West Virginia University as dean in 1927, and then on to Yale in 1930 where he remained until 1938. While at Yale, he published two interrelated books that present his distinctive perspective on politics and law, *The Symbols of Government* (1935) and *The Folklore of Capitalism* (1937). During the early years of the Roosevelt administration, Arnold became part of the New Deal “brain trust” and worked part time in a variety of positions. When Robert Jackson left the Antitrust Division to join the Supreme Court, Arnold was appointed his successor. At the Antitrust Division, Arnold pursued an aggressive enforcement strategy and built the Division into the major force that it remains. He served in that position from 1938 to 1943 when he was pushed out and appointed to the U.S. Court of Appeals for the D.C. Circuit. After an unhappy two years as a judge, Arnold resigned to found a law firm with Paul Porter and Abe Fortas that survives today as Arnold and Porter.

To understand how Arnold’s perspective on the law may help explain the politics of corporate law reform, it is useful to situate it among other ways of understanding the oft observed gap between rhetoric and reality. One common view – the “public interest” view – is that the significant gap between the efforts expended in bringing about regulatory change and the disappointing results arises because change is hard. With entrenched and effective interest groups, and imperfect human beings, progress is slow. Failures, on this view, should not obscure significant successes in which the public interest is advanced. The stridency of the rhetoric reflects the importance of the problem or the commitment of the contestants, whatever the ultimate (and modest or non-existent) effects. The frequent failures should be viewed as a spur to greater effort.

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3 For a very interesting biography, see Spencer Weber Waller, Thurman Arnold (2005).
4 Waller at 108—110.
5 Waller, Chapter 7.
The major contemporary competition for the “public interest” view is the “public choice” perspective. Public choice views contests over policy as attempts by well-focused interest groups to achieve private goals at the expense of other groups – what is often referred to as “rent-seeking” – while cynically garbing efforts in the rhetoric of the public interest. This “public choice” or “rent-seeking” view identifies a gap between rhetoric and reality, and views the main drivers as largely rooted in self-interested, economically motivated conduct. On this view, interest groups often proceed cynically in an attempt to gain private advantage, while the general public is largely deluded.

Thurman Arnold represents an additional and quite distinctive perspective. On his view, politics serves an entirely different function than it claims, a function that, unless recognized, will subvert reform efforts: law and politics are the “semi-sacred” ceremonies through which we make peace with the inherent but necessary contradictions between our ideals and reality. Although rooted in the Legal Realism that surrounded him at Yale in the 1930s, Arnold rejected its reformist anti-formalism as blind to “to the pervasiveness of symbols in the discourse of law and governance generally.” What distinguishes Arnold’s view is this “anthropological turn,” evident in his choice of the terms “folklore” and “symbols.” Arnold’s embrace of this anthropological approach, an outlook that was a prominent part of the general intellectual milieu

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7 An alternative approach, now largely ignored in corporate governance analysis, finds its roots in Marx. On this view, competitive political battles, indeed all of law, politics, culture and ideology, are viewed as largely epiphenomenal, with material economic relations (the base) “conditioning” or “determining” law, politics and ideology (the superstructure). Analytically, the problem with this approach is that the precise links between economic relations and the development of law, politics and ideology has never been spelled out with sufficient clarity to be analytically useful, at least in an area like corporate law. While it is easy enough to argue that the entire structure of corporate law and governance serves to legitimate the economic relations that constitute a market economy (indeed, it is indisputably true!), deploying this approach to analyze more fine-grained issues is not easy. In what follows, we largely ignore these approaches except insofar as we examine the “legitimation” function of corporate governance politics.
8 For a detailed and very insightful analysis of Arnold and the context in which he was writing, see Mark Fenster, The Symbols of Governance: Thurman Arnold and Post-Realist Legal Theory, 51 Buffalo L. Rev. 1053, 1070 (2003). In what follows, we rely heavily on his description.
9 In this regard, Arnold shared a view with others who had made the ideology of politics a topic for study, such as Harold Lasswell, Walter Lippman, Vilfredo Pareto and others. Murray Edelman picked up the theme decades later in Edelman, The Symbolic Uses of Politics (1964). For a brief overview of the literature, see Fenster, Thurman Arnold, at 1079-84; Fenster, Murray Edelman, Polemicist of Public Ignorance, 17 Critical Review 367. Although others focused on the symbolic aspect of politics, what makes Arnold so useful for our purposes is that he focused his critique, inter alia, on business law.
during the 1920s and 1930s, allowed for the possibility that the spectacle itself may be the point of the activity, and not just an incidental byproduct.

Writing during the Great Depression, Arnold was frustrated by the resistance to administrative/regulatory responses to the economic crisis and mass unemployment. He was particularly annoyed with the extent to which legal and economic concepts interfered with what he took to be sensible, necessary and practical responses. “The social needs were felt by everyone, but the slogans that the new organizations used had a queer sound. Therefore, the spirit of the Constitution, the traditional symbols of economics, and the general picture of a ‘rule of law’ as opposed to ‘bureaucratic control’ were all arrayed against them.”

But a standard “Legal Realist” debunking of conceptual analysis was not, for Arnold, sufficient. To make progress on social problems, Arnold thought, one must grapple with the hold that these concepts have on people. “We cannot be practical about social problems if we are under the illusion that we can solve them without complying with the taboos and customs of the tribe.” It is this combination – a legal realist’s skepticism about legal concepts combined with a practical politician’s understanding of the critical role of ritual and taboos in effecting change – that is most distinctive about Arnold’s view.

This led Arnold to adopt, at least rhetorically, an anthropologist’s external perspective. For Arnold, people “become bound by loyalties and enthusiasms to existing organizations” and, when successful, naturally view such organizations as representing moral and political perfection. This then leads them to adopt “creeds” that justify those organizations, and resist attacks on them. Arnold thus paid particular attention to the ways in which myths and ceremonies of various sorts are used to reconcile imbalances in power between individuals and the state and individuals and large firms.

For corporate law, three of the most important and useful chapters of *Folklore* are Arnold’s discussions of the myth of corporate personality (Chapter 8), the ways that Antitrust

10 Folklore at 2.
12 Folklore at 205.
13 Folklore at 10.
provides legitimating cover for monopoly (Chapter 9) and the ritual of corporate reorganizations (Chapter 10). In what follows, we quote liberally from Arnold’s analysis in order to give a sense of his distinctive voice and perspective.

For Arnold, the “personification of the corporation” was all about endowing large concentrations of economic power with the anti-regulatory benefits of nineteenth century rugged individualism. Our pioneer civilization, which formed a bedrock of American conceptions of legitimacy, was one “in which the prevailing ideal was that of the freedom and dignity of the individual engaged in the accumulation of wealth. The independence of the free man from central authority was the slogan for which men fought and died. This free man was a trader who got ahead by accumulating money.” But this ideal of rugged individualism clashed with the reality of large industrial organizations. “Indeed, the great organization in which most men were employees, and a few at the top were dictators, was a contradiction of that philosophy.”

How we came to terms with this contradiction between ideals and reality is what most interested Arnold. Because great organizations were inevitable, given technological progress, “nothing could stop the progress of such organization, and therefore in order to tolerate it, men had to pretend that corporations were individuals.” By identifying the great industrial organizations with the “dignities, freedom, and general ethics of the individual trader,” any move to break them up wholesale could be blocked. Just as some individuals are good and others bad, we could not expect that all great industrial organizations would be good. The bad ones could be punished without threatening the overall system. Moreover, “since individuals are supposed to do better if let alone, this symbolism freed industrial enterprise from regulation in the interest of furthering any current morality. The laissez faire religion, based on a conception of a society composed of competing individuals, was transferred automatically to industrial organizations with nation-wide power and dictatorial forms of government.”

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14 Folklore at 185-86.
15 Folklore at 187.
16 Folklore at 187.
17 Folklore at 189.
Arnold provides a wonderful 1936 quote from John W. Davis attacking the regulation of holding companies.\(^\text{18}\) What struck Arnold as notable was Davis’s attempt to rouse “his audience to a high pitch of indignation against an act regulating holding companies” by arguing as follows:

There is something in this act that arouses me far beyond the scope and tenor of the act itself. In one respect it is unique in the history of our legislation; in one respect it constitutes the gravest threat to the liberties of American citizens that has emanated from the halls of Congress in my lifetime. This is strong language. But I mean to make it so.\(^\text{19}\)

While the regulation of public utility holding companies was a reasonably important issue from both an antitrust and securities law perspective, a claim that the 1935 act constituted “the gravest threat to the liberties of American citizens” is laughable hyperbole.

Arnold was not suggesting that these myths could be dispensed with, only that we should not let them confuse us.

[This book] does not attack the use of the corporate personality in folklore. The results have been the creation of one of the greatest productive machines that the world has ever known, and this perhaps is justification enough if anyone is interested in justifying what has happened. This book is concerned only with diagnosing the present difficulties which have come upon us now that the industrial feudalism is no longer protecting large groups of our citizens who demand security, and with trying to explain the ideological difficulties which prevent the creating of organizations which will give that protection. We cannot be practical about social problems if we are under the illusion that we can solve them without complying with the taboos and customs of the tribe. The corporate personality is part of our present religion. Since, however, we must use the words and ceremonies, it becomes important that we be able to use them intelligently.\(^\text{20}\)

\(^\text{18}\) Public utility holding companies attracted substantial regulatory attention during the 1930s. With regard to the Public Utility Holding Act of 1935, see Report, SEC Division of Investment Management, The Regulation of Public-Utility Holding Companies (June 1995).
\(^\text{19}\) Folklore at X.
\(^\text{20}\) Folklore at 205.
In Arnold’s classic analysis of antitrust, he examined one of the “most important ceremonies which have dramatized the rugged individualism of business organizations.”21 It is also, as we shall see, suggestive for understanding corporate governance reform. Arnold’s analysis starts with a diagnosis that locates antitrust in a grand regulatory tradition:

This phenomenon is a familiar one and is constantly recurring in the growth of all social institutions. The simplest example is the institution of prostitution. We celebrate our ideals of chastity by constantly engaging in wars on vice. We permit prostitution to flourish by treating it as a somewhat minor crime and never taking the militant measures which would actually stamp it out. The result is a sub rosa institution which organizes the prostitutes after a fashion, at least to the extent that there never seems to be any shortage in our large cities.22

For Arnold, antitrust can best be understood as an example of the same sort of process: “Granted an insistent social demand, which opposes a deeply felt ideal, and a conflict of this kind between two institutions – one respectable and moral, exemplifying the ideal, the other sub rosa and nonrespectable filling the practical need – is as inevitable as the reaction of a man sitting on a hot stove.”23

As noted in Arnold’s chapter on the personification of the corporation, the conflict for which Antitrust was the solution started with a civic religion officially dedicated to the preservation of economic independence of individuals, of an industry made up of small competing concerns that, if not actual individuals, were at least identifiable with their owners. On this view, “bigness” was regarded as a curse because it led to monopoly and interfered with the operation of the laws of supply and demand. On the other hand, technological change and the emergence of specialized techniques made bigness essential to realizing economies of scale and scope, “to producing goods in large enough quantities and at a price low enough so that they could be made part of the American standard of living.”24 “In such a situation,” he wrote, “it

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21 Folklore at 205.
22 Folklore at 208.
23 Folklore at 209-10.
24 Folklore at 207.
was inevitable that a ceremony should be evolved which reconciled current mental pictures of what men thought society ought to be with reality.”25

In order to reconcile the ideal with the practical necessity, it became necessary to develop a procedure which constantly attacked bigness on rational legal and economic ground, and at the same time never really interfered with combinations. Such pressures gave rise to the antitrust laws which appeared to be a complete prohibition of large combinations. The same pressures made the enforcement of the antitrust laws a pure ritual. The effect of this statement of the ideal and its lack of actual enforcement was to convince reformers either that large combinations did not actually exist, or else that if they did exist, they were about to be done away with just as soon as right-thinking men were elected to office. Trust busting therefore became one of the great moral issues of the day, while at the same time great combinations thrived and escaped regulation.26

For all of his irony and acerbic cynicism, Arnold had a subtle appreciation of the value of ritual, and the dangers of taking that ritual too seriously:

Thus in those days anyone who attacked the “Trusts” could achieve the same public worship as a minister of the gospel who had the energy to attack vice. It was this that made Theodore Roosevelt a great man. Historians now point out that Theodore Roosevelt never accomplished anything with his trust busting. Of course he didn’t. The crusade was not a practical one. It was part of a moral conflict and no preacher ever succeeded in abolishing any form of sin. Had there been no conflict – had society been able to operate in an era of growing specialization without these organizations – it would have been easy enough to kill them by practical means. A few well-directed provisions putting a discriminatory tax on large organizations would have done the trick, provided some other form of organization was growing at the same time to fill the practical need. Since the organizations were demanded, attempts to stop their growth necessarily became purely ceremonial.27

Arnold does not underestimate Roosevelt’s accomplishment:

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25 Folklore at 207.
26 Folklore at 207-08.
27 Folklore at 211.
Theodore Roosevelt, with his big stick that never hit anybody, accomplished two things. First, he convinced the public that if we would only drive politics out of the Department of Justice the laws were sufficient to make these big individuals really compete. Second, he convinced corporate executives that it was a good thing to hire public relations counsel and show that they also were followers of the true religion. . . . The antitrust laws remained as a most important symbol. Whenever anyone demanded practical regulation, they formed an effective moral obstacle, since all the liberals would answer with a demand that the antitrust laws be enforced. Men like Senator Borah founded political careers on the continuance of such crusades, which were entirely futile but enormously picturesque, and which paid big dividends in terms of personal prestige.28

Arnold saved particularly savage condemnation for those poor well-meaning fools who would endeavor to make us live up to our articulated principles because doing so would destroy necessary institutions and cause serious social harm. Our institutional creeds, he emphasized, “must be false in order to function effectively. . . . Love of consistency and devotion to realism will wreck any institutional creed. When consistency is emphasized, conflicting ideals which may be very important in retaining loyalties have to be abandoned.”29 As with campaigns against prostitution, appeals to live up to our ideals should not be taken seriously: “The confusion accompanying most liberal reform movements is due to the fact that they are generally attempts to make the institution practice what it preaches in a situation where, if the ideal were followed, the function of the institution could not be performed.”30 Indeed, because “institutional doctrine is never a frank description of the practice and purpose of the institution . . . we who try to make institutions live up to their pretensions are the worst of executives. The history of human organization is strewn with the wreckage caused by people who tried honestly and sincerely to follow the logical implications of accepted doctrine.”31

28 Folklore at X.
29 Folklore at 356-57.
30 Folklore at 375.
31 Folklore at 378. One of the challenges of applying Arnold’s approach is how seriously to take it. As with any ironist, especially in print, it is not always clear when Arnold is ironic and sarcastic in criticizing benighted practices, or when he is serious in his approbation. In particular, Arnold’s critique of Antitrust, when juxtaposed with his aggressive enforcement stance as head of the Antitrust Division, might well suggest that his critique was directed at a particular era of lax antitrust enforcement – one that was hobbled by undue respect for myth and folklore – and not a rejection of Antitrust more generally. Cite to Spencer Waller biography? For our purposes, which are generally descriptive, the normative point of his arm chair anthropology can be set to one side, in favor of
Murray Edelman, some thirty years later in his seminal work, *The Symbolic Uses of Politics*, carried a very similar approach into the political turmoil of the 1960s. Like Arnold, Edelman viewed politics as symbolic and spectacular, an effort to reassure the masses, to induce quiescence and to preserve the status quo: “Political forms thus come to symbolize what large masses of men need to believe about the state to reassure themselves. It is the needs, the hopes, and the anxieties of men that determine the meanings.” At the same time, of course, political decisions also allocate goods, services and power. “There is accordingly no reason to expect that the meanings will be limited to the instrumental functions the political forms serve. The capacity of political forms both to serve as a powerful means of expression for mass publics and to convey benefits to particular groups is a central theme of this book.” Symbolic politics, then, can, but need not be accompanied by interest group rent-seeking.

In this Article, we try on a Thurman Arnold and Murray Edelman frame of mind to see whether this approach has utility in understanding corporate governance politics. In the next part, we review a selection of high profile corporate governance battles of the last decade or two: shareholder proposals to control the use of poison pills; proxy access; majority election of directors; mandatory shareholder proposals; and the battle over supermajority voting bylaws. For each, we review the substance of the issue, the rhetoric employed by the contestants, and the practical issues at stake. In each case, we find the tell-tale gap between rhetoric and reality that raises the question whether something else could be going on (or whether the contestants and their parties are simply mistaken).

Having concluded in Part II that the explicit stakes cannot explain the vigor of the contest, in Part III we consider a variety of alternative explanations for that gap. First, and most obviously, participants (leaders and followers) may simply be mistaken. Although this is implausible for most of the “leaders” of the various factions, it is more plausible for the foot-soldiers. Second, we consider a variety of “public interest” explanations that could explain the gap including the possibility that an issue is a proxy for something else, either because principle matters or because a battle becomes a “show of force.” We then consider various “public

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32 On Edelman’s debt to Arnold, see Symbolic Politics at p. 40.
34 Edelman at 2.
In Part IV, we consider some of the implications of this view of corporate governance politics. If we cannot take the intensity of corporate governance reform battles as a reliable indicator of the significance of the issue being debated, how should investors, managers and directors and the general public react? If we become convinced that corporate governance reform is rather like the antitrust or anti-vice campaigns in Thurman Arnold’s description, what follows?

**Part II: Some Illustrative Corporate Governance Controversies**

An interesting feature of corporate governance politics is that there seem to be new controversies every year. Although there is a certain amount of uncertainty regarding the high profile issues, there is significantly less uncertainty as to the prominent protagonists. The one sure thing is that we will never have a year in which nothing happens. It is almost enough to make one imagine that there is a corporate governance reform “industry” that demands activity to keep itself going.

In this Part, we contrast rhetoric and reality in a variety of corporate governance controversies. In what follows, we will say that activism has a significant “symbolic” element when it cannot be fully explained by the material stakes at issue in a given controversy.

1. **Poison Pill Proposals**
   
   (a) The Issue

   One of the most common shareholder proposals asks boards to redeem a poison pill or to submit it to a shareholder vote. A 2000 shareholder proposal at Baxter International is typical:
RESOLVED: The shareholders of Baxter International Inc. ("Company") request that the Board of Directors redeem the stock purchase rights issued December 9, 1998, unless said issuance is approved by the affirmative vote of a majority of the outstanding shares at a meeting of shareholders held as soon as practicable.\(^{35}\)

According to Georgeson, which compiles data on corporate shareholder proposals filed in S&P 1500 firms, poison pill proposals were the most common type of proposal filed in the 1987 to 2004 period.\(^{36}\) These proposals also tend to garner substantial support from shareholders. Thus, for example, during the 2000 proxy season, the average poison pill rescission proposal was supported by 55% of the shares voted, with 39% voting against and 6% abstaining.\(^{37}\)

(b) The Rhetoric

Poison pills are widely regarded as the most formidable takeover defense. As long as a modern poison pill is in place, a company is virtually takeover-proof.\(^{38}\) As explained by Marty Lipton, “[The poison pill] is an absolute bar to a raider acquiring control … without the approval of the company’s board of directors.”\(^{39}\)

Because of this potency, governance professionals at major institutional investors view pills as illegitimate unless approved by shareholders. The State of Wisconsin Investment Board, for example, has a policy to “vote for shareholder proposals that ask a company to submit its poison pill for shareholder ratification”\(^{40}\) Vanguard’s proxy voting guidelines state that “[i]n general, shareholders should be afforded the opportunity to approve shareholder rights plans within a year of their adoption.”\(^{41}\) T. Rowe Price notes that “[w]e routinely vote against directors

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\(^{35}\) http://www.sec.gov/Archives/edgar/data/10456/000095013100001926/0000950131-00-001926.txt

\(^{36}\) GEORGESON, ANNUAL CORPORATE GOVERNANCE REVIEW (1987-2004). Poison pill proposals started to decline as shareholder activism caused a reduction in outstanding pills. See, GEORGESON, ANNUAL CORPORATE GOVERNANCE REVIEW 6 (2007).

\(^{37}\) GEORGESON, ANNUAL CORPORATE GOVERNANCE REVIEW 6 (2000). Additionally, in 2004, the last year poison pill proposals were the most common type of proposal, such proposals were supported by 60% of the shares that voted on the proposal, with 37% voting against and 3% abstaining. GEORGESON, ANNUAL CORPORATE GOVERNANCE REVIEW 6 (2004).

\(^{38}\) See John C. Coates, Takeover Defenses in the Shadow of the Pill: A Critique of the Scientific Evidence, 79 TEX. L. REV. 271, 320 & n.195 (2000) (stating that poison pills prevent bidders, who cannot win a proxy contest for the target, from acquiring more than a small percentage of target stock because they will be unable to redeem the pill).

\(^{39}\) See Martin Lipton, Wachtell, Lipton, Rosen & Katz, Memorandum to Clients (Jan. 15, 1993).

\(^{40}\) See http://www.swib.state.wi.us/proxyvoteS.pdf, p. 21.

\(^{41}\) See https://investor.vanguard.com/about/vanguards-proxy-voting-guidelines.
of any company that adopts a poison pill without subjecting it to shareholder approval, and we support shareholder proposals calling for companies to offer shareholders an opportunity to ratify their poison pills."\(^{42}\)

Unsurprisingly, less mainstream shareholder activists pick up on these themes. Thus, union activist UNITE HERE,\(^{43}\) the shareholder proponent of the Baxter proposal (and holder of 10,400 of the company’s shares), argued that “shareholders should have the right to vote on the necessity of such a powerful tool that could be used to entrench existing management” and that “we do not believe that our Company should maintain its management and board-entrenching poison pill Rights Agreement without shareholder approval.” It concluded that in light of “the undeniably undemocratic way in which they were assigned to shareholders, we believe these rights should lapse and not be extended, renewed or issued again without a shareholder vote.”\(^{44}\)

Boards take shareholder proposals to redeem poison pill seriously. After such proposals received majority support, several companies let the poison pills they had in place expire.\(^{45}\) Without a poison pill, a company’s ability to resist a hostile takeover would be substantially weakened. By inducing companies to let their poison pills expire, activists thus scored a major victory. Or did they?

(c) The Reality

The reality is that poison pill proposals, including the ones that induced companies to terminate or not to renew existing pills, have no impact on the company’s ability to resist a bid. As any corporate lawyer worth her salt can tell you, it is legally and practically irrelevant whether a company has a poison pill in place when a hostile bid is made. Poison pills are adopted unilaterally by a board and do not require any shareholder approval.\(^{46}\) If needed, a reasonably competent lawyer can implement a “rights plan” - the formal name for a pill – within


\(^{44}\) [http://www.sec.gov/Archives/edgar/data/10456/000095013100001926/0000950131-00-001926.txt](http://www.sec.gov/Archives/edgar/data/10456/000095013100001926/0000950131-00-001926.txt).


\(^{46}\) Coates at 288 n.62.
a day. Hostile bids, by contrast, take time to consummate. The Williams Act requires that tender offers be left open for a period of at least 20 business days and mandates that any shareholder who acquires more than 5% of the company’s stock make a disclosure within 10 days. This affords potential targets plenty of time to adopt a pill once a pill is needed. Raiders, of course, are just as aware of this fact as are the boards of potential targets.

Terminating or not renewing a pill does not represent an explicit or implicit commitment by the board not to adopt a pill in the future. In fact, in all likelihood, a board could not validly bind a future board not to adopt a pill if the future board believed that adopting a pill was in the company’s best interest. So why do shareholder activists submit proposals asking boards to redeem poison pills and then lobby for them?

2. Proxy Access

(a) The Issue

Up to two years ago, one of the most-sought after – and most fought-over – corporate governance reforms was proxy access. In 2003, the SEC released a proposal to grant shareholders access to the corporation’s proxy statement following a triggering event - either a 35% or more “withhold” vote in a director election or a majority vote by shareholders electing to make the company subject to proxy access. Under that proposal, after a trigger, shareholders of any publicly traded company who held at least 5% of the company’s stock for a minimum of two years would have been able to make nominations for some of the board seats.

Despite strong backing by shareholder activists and many institutional investors, the proposal was not adopted. Instead, in 2007, the SEC restricted the ability of shareholders to

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47 Katz & McIntosh, supra note __, at 5.
49 Katz & McIntosh, supra note __, at 5 (noting that 20% of pills are adopted in response to specific threat).
50 See Quickturn Design Sys., Inc. v. Shapiro, 721 A.2d 1281 (Del. 1998).
53 See the following comments to Security Holder Director Nomination, 68 Fed. Reg. 60,790: William C. Thompson Jr., New York City pension funds and retirement systems (Dec. 16, 2003) (calling the proposal “one of the most...
seek proxy access on a company-by-company basis through a shareholder proposal under Rule 14a-8.  

After the election of President Obama, the SEC’s composition, and its view on proxy access, changed again. In 2010, with the continued support of many activists and institutional shareholders, it adopted a proxy access rule that went beyond the 2003 proposal: it removed the

significant actions taken to reform corporate governance and restore investor confidence”), Gary Findlay et al., 38 Public Retirement Sys. 1 (Dec. 22, 2003) (stating that the proposed rules would give shareholders “the ability to participate meaningfully in board elections” for the first time), Peter C. Clapman, Teachers Ins. & Annuity Ass’n of America Coll. Retirement and Equities Fund 1 (Dec. 17, 2003) (stating that the rule “would provide security holders with the ability to play a more direct and effective role in nominating and electing directors”), Peter M. Gilbert, Pa. Emps. Retirement Sys. 1 (Dec. 22, 2003) (the rules will “enable the shareholders, the true owners of the corporation, to hold boards of directors . . . more responsive”), Keith Johnson, Wisc. Inv. Bd., Inc. 2 (Dec. 22, 2003) (stating that the proposal will “improve the quality of director candidates through greater competition and attention to credentials”), Marsha D. Richter, L.A. County Emps. Retirement Ass’n, (Dec. 20, 2004) (“improving shareholder access to the proxy process is the most important corporate governance issue facing investors today”), Laurie Fiori Hacking, Ohio Pub. Emps. Retirement Sys. (Dec. 10, 2004) (calling the proposal “one of the most significant and important investor reforms adopted by the SEC since it adopted Rule 14a-8”), Alan G. Hevesi, New York State Common Retirement Fund 1 (Dec. 18, 2010) (stating proxy access is of “critical importance” especially when considering recent corporate scandals), Gerald W. McEntee, AFSCME 2 (Dec. 24, 2003) (stating that the proposal would “restor[e] accountability to our system of corporate governance”), Sean Harrigan, CalPERS 1 (Dec. 5, 2003) (the proposal “is perhaps the most significant reform to come as a result of the financial crisis in the U.S.”) (available at http://www.sec.gov/rules/proposed/s71903.shtml); Andrew G. Murphy, Alliance Capital (Dec. 16, 2003) (supporting the proposal as “a means of improving corporate governance, increased director accountability, independence, and performance.”), Gabriel P. Caprio, Amalgamated Bank (Dec. 22, 2003) (stating the proposal “represents an important step toward meaningful reform of shareholder access rules.”), Richard L. Trumka, AFL-CIO 2 (Dec. 19, 2003) (“granting long-term shareholders a meaningful say in picking directors is the most important investor reform to be considered by the commission in decades”), someone, Int’l Brotherhood of Teamsters 1 (Dec. 23, 2003) (the proposal “is perhaps the single most important issue currently before the Commission and has the potential to produce true and lasting reform”) Henry H. Hopkins, T. Rowe Price Assocs. (Dec. 24, 2003), Amy B.R. Lancellotta, Inv. Co. Inst. (Dec. 22, 2003) (available at http://www.sec.gov/comments/s7-10-09/s71009.shtml); Jack Ehnes, CalSTRS 2 (Jan. 19, 2010) (stating that “[p]roxy access will finally give shareholders a meaningful voice in the nomination process and will be the greatest advancement of shareholder rights in decades”), Meredith Williams, Colorado Pub. Employees’ Retirement Ass. 2 (Jan. 19, 2010) (stating that “[a]mending proxy access rules will provide for the exercise of shareholders’ fundamental rights to nominate and elect directors”), Denise L. Nappier, Connecticut Retirement Plans & Trust


55 See the following comments to Facilitating Shareholder Director Nominations, 33 Fed. Reg. 9086: Gerald W. McEntee, AFSCME 3 (Jan. 19, 2010) (“shareholders need a uniform federal proxy access rule to facilitate their key state-law right to nominate and elect directors who will robustly represent their interests.”), Cornish F. Hitchcock, Amalgamated Bank LongView Funds 2 (Aug. 17, 2009) (“the current economic crisis has only underscored the need for shareholders to be able to hold directors accountable . . . by nominating candidates whose merits can be considered by all shareholders when they review the company-prepared proxy materials.”), Mark R. Manley, AllianceBernstein 2 (Aug. 14, 2009) (supporting “the central problem that needs to be solved – shareholders limited ability to exercise their rights to nominate directors and have the nominations disclosed to and considered by shareholders.”), Joseph A. Dear, CalPERS (Aug. 14, 2009) (calling the new rule “historically significant reform that will enable investor to hold corporate boards accountable and restore investor confidence in capital markets.”), James P. Hoffa, Int’l Brotherhood of Teamsters 2 (Aug. 17, 2009) (calling rules allowing shareholders to nominate board candidates “the most meaningful way to empower shareholders”) (available at http://www.sec.gov/comments/s7-10-09/s71009.shtml); Jack Ehnes, CalSTRS 2 (Jan. 19, 2010) (stating that “[p]roxy access will finally give shareholders a meaningful voice in the nomination process and will be the greatest advancement of shareholder rights in decades”), Meredith Williams, Colorado Pub. Employees’ Retirement Ass. 2 (Jan. 19, 2010) (stating that “[a]mending proxy access rules will provide for the exercise of shareholders’ fundamental rights to nominate and elect directors”), Denise L. Nappier, Connecticut Retirement Plans & Trust
requirement of a triggering event and reduced the threshold for nominations to 3% held for three
years. 56 Even though Congress, as part of the Dodd-Frank Act, specifically authorized the SEC
to regulate proxy access, the proxy access rule was struck down by the Court of Appeals for the
DC Circuit in Business Roundtable v. SEC. 57 The Court, however, left in place a companion rule
that reversed the 2007 rule and specifically permitted shareholders to seek proxy access on a
company-by-company basis through a shareholder proposal under Rule 14a-8. 58

(b) The Rhetoric

From the SEC’s original proposal in 2003 through the invalidation of the SEC’s revised
proxy access rule in 2011, proxy access excited great controversy. To opponents, proxy access
posed a clear and present danger to American prosperity. The Chamber of Commerce included
killing proxy access among its top five priorities; 59 SEC Commissioner Casey thought it was
“fatally flawed”; 60 two Wachtell lawyers feared it would “wreak havoc with American
business,” 61 while Willkie Farr & Gallagher thought it would merely have a “profound effect on
the election of directors.” 62

Proponents adopted equally strong rhetoric in the other direction. CtW Investment
Group, a proxy advisory firm, called proxy access a “new and powerful tool”; 63 the Council of
Institutional Investor thought it was “groundbreaking for U.S. shareowners”; 64 SEC

adequately address the rule’s economic effects, the rule was “arbitrary and capricious”).
58 See Id. at 1153, n.
60 Id. at 1622 (quoting SEC Commissioner Kathleen Casey).
61 David A. Katz & Laura A. McIntosh, Senate Bill Adversely Affects the Landscape, N.Y. L.J., May 27, 2010, at 5;
see also Martin Lipton, Some Thoughts for Boards of Directors in 2008, Dec. 6, 2007, at 6 (calling proxy access “a
serious mistake with far reaching consequences”).
62 Willkie Farr & Gallagher, SEC Proposes “Proxy Access” Rules to Facilitate Director Nominations by
Shareholders, Client Memorandum, June 23, 2009
Commissioner Walters felt it would “restore shareholder confidence”\(^{65}\), Commissioner Goldschmid worried that, without proxy access, shareholders would remain “marginalized in choosing the direction of boards”\(^{66}\), and CalPERS regarded “[p]roxy access [as] one of our top priorities.”\(^{67}\)

(c) The Reality

The 2012 proxy season was the first time that shareholder activists had a clear opportunity to seek implementation of proxy access through a shareholder proposal. The SEC rules that had been unclear (prior to 2007) or had been clear in not permitting such proposals (between 2007 and 2011) had been revised.\(^{68}\) Moreover, in the meantime, Delaware modified its law to clarify that proxy access could be validly adopted via a by-law amendment.\(^{69}\) This presented the possibility of passing a “mandatory” Rule 14a-8 proposal, that directly amends the by-laws to grant proxy access (rather than merely requests the board to take steps to implement proxy access). Finally, by 2012, it was clear that the SEC would not take up “proxy access” in the near future.\(^{70}\)

Viewed from this perspective, shareholder activists had merely lost a battle, but not the war, when the SEC’s proxy access rule was invalidated in *Business Roundtable*. To be sure, the battleground has shifted to the ballot box, but the investor community had been sensitized to, and had given significant support to some version of, proxy access. Thus, activists had reason to be optimistic over how a proxy access shareholder proposal would fare. Surely they would avail themselves of the opportunity to pressure companies to implement proxy access – their long sought and critically important governance reform -- through actual or threatened 14a-8 proposals.

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\(^{65}\) Walter Calls for Action on Proxy Access, Disclosure, Other Governance Topics, Corporate Law Daily (BNA) (Feb. 19. 2009), http://0-news.bna.com.pacman.law.du.edu/cldn/display/batch_print_display.adp?searchid=14113940 (attributing phrase to SEC Commissioner Elisse Walter).\(^{XE}\) this is an online only source and you can only access it with a password through BNA].


\(^{67}\) http://www.calpers.ca.gov/index.jsp?bc=/about/press/pr-archive/pr-2011/july/proxy-access-case.xml

\(^{68}\) 17 CFR 240.14a8 (revisions effective as of Sept. 20, 2011).


So what happened on the proxy access front in 2012? Not much. U.S.-based institutional investors, many of which had been strong advocates of the SEC proposal, submitted a total of three proxy access proposals: at Hewlett-Packard (submitted by Amalgamated Bank); at Chesapeake Energy (by New York City pension funds); and at Nabors Industries (by a group of pension funds). Others, including several individual shareholders and the Norway-based Norges Bank, submitted another 23 proposal. Of these, however, eight were omitted because they failed to comply with SEC rules and one was not presented at the meeting. As tabulated by Georgeson, proxy access was only the 10th most common type of shareholder proposal (with 6 entries among the S&P 1500) and only about half as common as the 9th (Cumulative Voting, with 11 entries).71

Perhaps activists feared that the overall shareholder support for proxy access was not, in fact, high. So once they lost the political battle to obtain proxy access through a SEC rule, they did not even bother to fight the battle to obtain proxy access through the ballot.

We do not think so. In the few companies where proxy access shareholder proposals came to a vote, they did reasonably well. Of the twelve proposals for which we could obtain data, six were supported by ISS, the most influential proxy advisor, and eight were supported by Glass Lewis, the second most influential advisor. The four proposals by Norges Bank garnered 25-30% of the votes including abstentions (30-39% of the votes excluding abstentions), a reasonably successful result for 14a-8 proposals. Importantly, the Norges Bank proposal went substantially beyond the SEC rule by granting proxy access to holders who held a minimum of 1% of the company’s stock for a 1 year period (as opposed to 3% for 3 years). A less broad proposal may well have attracted greater support. To be sure, the proposals made by individual shareholders, some of which granted proxy access to an even wider group, did less well.

Most importantly, however, the three proposals made by U.S.-based institutional investors, which resembled the SEC rule, did extraordinarily well. The two proposals that came up for a vote were supported by ISS and by Glass Lewis; the proposal at Nabors received support from 56% of the votes including abstentions (56.2% of the votes excluding abstentions); the proposal at Chesapeake Energy did even better, garnering the support of 59.9% of the votes including abstentions (62.3% of the votes excluding abstentions). The third proposal, at Hewlett-

71 See GEORGESON, ANNUAL CORPORATE GOVERNANCE REVIEW 18 (20012).
Packard, was withdrawn after the company agreed to recommend to shareholders a proxy access proposal that would be submitted for a vote at the 2013 meeting\(^{72}\) where it was approved by an overwhelming majority.\(^{73}\) While Nabors, Chesapeake, and Hewlett-Packard faced other management problems that may have increased shareholders’ willingness to support proxy access (and the board’s willingness to settle), the outcome for these companies makes it hard to believe that a proxy access proposal with terms similar to those in the SEC Rule would not also have succeeded in many other companies.

The 2013 experience was similar. As of the end of July, only 12 shareholder proposals on proxy access had come up for a vote. Other than Norges Bank (which submitted three proposals), institutional investors remained largely on the sidelines. Of the five proposals that resembled the SEC rule, three received more “for” than “against” votes\(^{74}\) and a fourth received 40% support.\(^{75}\) In addition to Hewlett Packard, Chesapeake Energy submitted its own proposal on proxy access, which passed with a large majority. As in 2012, none the seven 2013 proposals that had more liberal thresholds for nominations garnered a majority (though those submitted by Norges obtained approximately one-third of the affirmative votes).\(^{76}\)

What explains, then, why shareholder activists made such a strong push to get proxy access adopted by the SEC, but then failed to lift a finger to get it adopted through shareholder resolutions? In an earlier article, we argued that proxy access would have had a trivial impact on corporate governance. Conceivably, activists read our article and realized that they had, for the prior decade, focused their energy on the wrong reform. As much as we like to believe that, we doubt it is true. Why, then, were they fighting?

3. **Majority Voting**

(a) The Issue

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\(^{72}\) [http://online.wsj.com/article/SB10001424052970204662204577201743734220890.html](http://online.wsj.com/article/SB10001424052970204662204577201743734220890.html)

\(^{73}\) [http://www.sec.gov/Archives/edgar/data/47217/000004721713000012/annualmeeting_032013.htm](http://www.sec.gov/Archives/edgar/data/47217/000004721713000012/annualmeeting_032013.htm).

\(^{74}\) The proposals were made at Verizon, CenturyLink, and Nabors./

\(^{75}\) The proposal was made at Walt Disney. The fifth proposal, at Microwave Filter, received only 15% support.

\(^{76}\) The seven proposals were made at Bank of America, iRobot, Goldman Sachs, Staples, Netflix, Charles Schwab, and CME Group.
The traditional voting standard, which applies as a default rule in Delaware and most other states, is that directors are elected by a plurality of the votes cast.\textsuperscript{77} The problem with the traditional plurality standard is that it has little meaning in an uncontested election, as most board elections are. If the number of nominees to the board is equal to the number of board seats to be filled, every nominee who receives even one vote is elected.\textsuperscript{78} As a result, a nominee can be elected even if the vast majority of shareholders are opposed.

In response, beginning in 2005 (and continuing to the present), shareholder activists began to push for changes in the voting standard. Initially, the plurality standard was supplemented by a board policy requiring each member or board nominee to submit a conditional offer to resign if the director did not receive a majority of the votes cast at the next election.\textsuperscript{79} As many activists were still not satisfied, many companies amended their by-laws or to their certificates of incorporation to adopt a majority standard for election.\textsuperscript{80} The Council of Institutional Investors identifies majority voting as a priority and has recently pushed Delaware, the NYSE and NASDAQ to adopt it as either a mandatory rule or default rule for uncontested elections.\textsuperscript{81}

(b) The Rhetoric

For shareholder activists, majority voting is a dream issue. The traditional plurality system, in which it is theoretically possible for a director to be elected by a single vote against the overwhelming opposition of shareholders, offends basic notions of “shareholder democracy.” Elections with plurality voting were described as “rubber stamp elections [that] are unlikely to shape director behavior in favor of long-term shareholders.”\textsuperscript{82} Though plurality voting is commonly employed in the U.S., including in Congressional races, arguments against it were filled with references to elections in the old Soviet Union: “Investors may think they live in the United States of America, but when it comes to electing corporate directors -- shareholders'
intended watchdogs in the boardrooms -- they are definitely back in the U.S.S.R. Even sadder to say, some of the nation's biggest mutual funds are helping to keep them there."\(^{83}\)

Activists also promised that a shift to majority voting would genuinely empower shareholders:

“Director accountability is the hallmark of good governance,” said Dr. Martha Carter, ISS’ director of U.S. Research. “The board election process must ensure that shareholders' expressions of dissatisfaction with the performance of directors have meaningful consequences. A majority vote standard transforms the director election process from a symbolic gesture to a meaningful voice for shareholders.”\(^{84}\)

Opponents were equally engaged and argued that a shift from plurality to majority voting would threaten significant negative consequences:

Majority voting would give special-interest shareholder activists increased opportunity to pursue their particular objectives, in many cases to the detriment of other shareholders and the company as a whole. Activists would gain leverage from the ability to defeat a director nominee even if withheld votes constituted substantially less than a majority of the outstanding shares. Moreover, the functioning of the board would be disrupted if a key director did not win re-election; if the board had to function for a period of time without a full complement of members; or if top director candidates were deterred from participation by the potential embarrassment and reputational effects of “losing” an election.\(^{85}\)

(c) The Reality


\(^{84}\) Institutional Shareholder Services Takes Stand on Majority Vote Standard, March 11, 2005, PRNewswire (available on lexis). For more, see the ISS Institute for Corporate Governance, Majority Voting in Director Elections: From the Symbolic to the Democratic (2005) available at: google title. The Council of Institutional Investors, in a August 11, 2011 letter to the Delaware Bar Association’s Section on Corporate Law, proposed amended the Delaware GCL to make majority voting the default setting and sounded similar themes: “The benefits of a majority vote standard are many: it democratizes the corporate electoral process; it puts real voting power in the hands of investors with minimal disruption to corporate affairs; and it makes boards’ more representative of, and accountable to, shareowners.”

\(^{85}\) David Katz and Laura McIntosh, Corporate Governance: Majority Election of Directors at 3-4, March 24, 2005 WLRK memo, available at [google for link]
Once shareholder activists highlighted the undemocratic features of the plurality election system, the system began to collapse. Large companies quickly moved to change the voting rules governing the election of directors. Within less than two years, between February 2006 and November 2007, half of the S&P 500 companies moved from plurality voting to some form of majority voting.86 Although, for smaller companies, the pace of change has been slower, by 2012, 52% of midcap and 19% of smallcap companies had adopted majority voting.87

We do not claim that a move from a plurality standard to a majority regime is meaningless. We do claim, however, that the “problem” of powerless shareholders under the plurality standard is not so big, that the solutions generated by the offer to resign policy and the majority standard do not empower shareholders all that much, and that the plurality standard has certain advantages over a majority regime. The net effect of a move from one standard to another is, in our assessment, small. Why, then, such a big fight?

Consider first the “problem” generated by the plurality standard. To keep the problem in perspective, it is important to note that the vast majority of director nominees in uncontested elections are elected with a majority – in fact, usually well over a majority – of the votes cast. For example, in the 2009 proxy season, only 82 director nominees for a Russell 3000 company failed to receive a majority “for” votes; in the 2008 season, the respective number was 31.88 Thus, the difference in voting standards affects only a small number of nominees each year. Second, significant withhold votes, even if far short of a majority, are regarded as an embarrassment and often result in some corporate response. Third, responses are usually forthcoming for nominees that receive a majority of withhold votes even if the company at issue subscribes to the traditional plurality standard for election. In an earlier study, we found that for about 70% of directors who received majority withhold votes, the company’s response, usually within one year of the vote, was deemed satisfactory by shareholders.89 For example, when the high withhold vote is due to the board adopting a poison pill or to a director not being sufficiently independent due to business relations with the company, the company may then

86 See Claudia H. Allen, Study of Majority Voting in Director Elections, Neal, Gerber & Eisenberg, LLP, Nov. 2007 (from Feb. 2006 to Nov. 2007, percent of S&P 500 companies with majority voting increased from 16% to 66%).
87 See letter, supra not __, at 3.
89 Id. at 1421.
repeal the pill or the director may terminate the business relationship. When this occurs, the
director will typically be re-elected with a clear majority the following year. In most of these
cases, however, the response did not take the form of pressuring the director to resign or not re-
nominating her. In sum, majority withhold votes are rare events; if they happen, they usually
result in change in policy even under a plurality standard; but they rarely result in a change in the
board.

To see how a majority regime affects this “problem,” we start by examining the direct
effect of the different standards for a nominee who failed to receive majority support. Under the
plurality standard, the nominee is elected. Under the offer to resign policy, the nominee is also
elected, but the other board members can accept (or not accept) her offer to resign. In other
words, it is up to the other board members whether the nominee retains her board seat. Under
the majority standard, the nominee is not elected. However, under the law of Delaware and other
states, a director serves until her successor is elected or she resigns or is removed.90 If the
nominee is already a board member, she will thus retain her seat for the time being until she
either resigns or the board elects someone else to the quasi-vacant seat. The board, of course,
may not act at all or could appoint the very nominee who failed to receive a majority shareholder
vote to fill the vacancy generated by her non-election. In other words, just as in the offer to
resign policy, it is up to the other board members whether the nominee retains her board seat.
From this vantage point, the offer to resign policy and the majority standard are equivalent, and
different from the plurality standard. But the plurality standard is not as different as it appears.
Though the other board members cannot force a nominee who is validly elected to resign, they
can put significant pressure on her and, of course, they can refuse to nominate her when her term
is up. As a practical matter, even under the plurality standard, the other board members have
significant influence over whether the nominee retains her board seat and ultimately control over
how long she does so.

To be sure, the description of the direct legal effect of the different standards does not do
full justice to the actual differences. A board may be more reluctant to appoint a nominee who
failed to receive a majority vote under a majority standard to the vacancy created by her non-
election than to reject the offer to resign of a nominee who failed to receive a majority vote under

90 Del. Code Ann. tit. 8, § 141(b).
an offer to resign policy. Similarly, boards may be more reluctant to reject an offer to resign than to fail to pressure a nominee to resign on her own accord. Thus, as a practical matter, a majority withhold vote is more likely to result in a change in board composition under a majority regime than under plurality voting.

But the different reaction of a board to a majority withhold vote reflects the fact that withhold votes send a different message depending on the applicable voting standard. On one hand, a majority withhold vote, when a company subscribes to a plurality standard, asks the company to fix some problem, but conveys the message that it is all right to keep the director on the board if the problem is fixed. In our study, we found that when the board fixed the problem that accounted for the majority withhold vote under plurality voting, the director who received the majority withhold vote gained large shareholder support at the next election. Shareholders, in other words, did not mind the fact that the director did not resign as long as the problems were fixed. On the other hand, a majority withhold vote, when a company subscribes to a majority standard, sends the board a stronger message to get rid of the director. It would thus be wrong to look at the consequences of a majority withhold vote under a plurality standard and conclude that the plurality standard is deficient because most directors who receive a majority withhold vote retain their seats.

Any individual company, of course, can only have one voting standard for the election of directors. From a governance perspective, therefore, there is a choice of which type of message shareholders want to be able to send. It would be reasonable for shareholders to prefer a plurality standard because they think that being able to send the message to fix a problem is more important, either because they care more about fixing the underlying problem than changing the board composition, or because the issue may arise more frequently, or because it may be easier to garner a majority withhold vote under a plurality standard than under a majority standard.

One possible interpretation of the push by shareholder activists for a majority standard, and the quick and widespread success they have attained, is that it reflects a conscious choice by shareholders that it is much more important to be able to send the message conveyed by a majority withhold vote under a majority standard than the one conveyed by a majority withhold vote under a plurality standard.

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91 Kahan & Rock, supra. Note __.
vote under a plurality standard. This is possible although, given the very subtle differences between messages sent under different voting standards, it is unlikely to explain the highly charged rhetoric summarized above. Are there more plausible explanations for why activists push for a majority voting standard, why boards have overwhelmingly given in without a fight, and why a pillar of Delaware corporate law like former Chief Justice Norman Veasey proposed a version of majority voting?92

4. The Scarcity of Mandatory Proposals

(a) The Issue

One of the shareholder proposals that received the most attention during the 2013 proxy season was the resolution, introduced by the AFSCME Employees Pension Plan, to separate the role of CEO and Chairman of the Board at J.P. Morgan Chase.93 The target of the proposal was J.P. Morgan’s high-profile CEO (and Chairman) Jamie Dimon. Dimon had received plaudits for steering his company relatively unscathed through the financial crisis, but more recently had been criticized for his handling of the “London Whale,” who accumulated over $5 billion in trading losses for the bank.94 In the closing days of the voting period, with several institutional investors still making up their minds on how to vote, Dimon suggested that he might resign if the proposal were adopted, a comment interpreted by some as a threat.95

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92 See description of Veasey’s role and views are available in ISS Institute for Corporate Governance, Majority Voting in Director Elections: From the Symbolic to the Democratic, the ISS Institute for Corporate Governance, in WHAT ALL BUSINESS LAWYERS & LITIGATORS MUST KNOW ABOUT DELAWARE LAW DEVELOPMENTS 2006, 331–75 (PLI Corp. L. & Prac., Course Handbook Series No. 1543, 2006) at pp. 6, 9, 18 and nn. 20, 25, and 29. (also available at: http://maga.econ.msu.ru/Work/%D0%A1%D0%A8%D0%90%20-%20Presentations/Majority_Voting_White_Paper.pdf).
Proposals like AFSCME’s can be introduced either as precatory resolutions or as mandatory bylaw amendments. Precatory proposals, of course, are non-binding. Boards are at liberty to ignore them. Although boards nowadays pay much more attention to precatory resolutions than they used to, a significant percentage are not implemented.96

Some resolutions, such as those requiring a charter amendment for implementation, can only be offered as precatory resolutions. Other resolutions involve a subject matter that is so complex that it cannot be squeezed into the 500 word limit imposed by Rule 14a-8.97 For those, a precatory resolution setting forth a broad goal and leaving it to the board to work out the detail may be the best realistic alternative.

In principle, however, most subject matters that can be regulated through a bylaw provision can be introduced as a mandatory bylaw amendment under Rule 14a-8. One might expect that shareholders would not rely on the good will of boards, who by definition are opposed to the resolution as a substantive matter, if they do not have to. Offering and passing a precatory resolution, when a mandatory bylaw resolution is permitted, is thus puzzling.

(b) The Rhetoric

Shareholder activists, of course, complain when boards ignore precatory resolutions that receive majority shareholder support.98 They have also long bemoaned the lack of shareholder influence over the rules on corporate governance. The intellectual origins of the criticisms date back to then Columbia law professor (and former SEC chair) William Cary who argued that state competition to attract incorporations results in a “race to the bottom.”99 More recently, Harvard law professor Lucian Bebchuk has complained that “U.S. corporate law has long denied

96 See Marcel Kahan & Edward Rock, Embattled CEOS, 88 TEX. L. REV. 987, 1012-13 (2010) (stating that although the share of precatory resolutions implemented by boards rose from 20% in 2001 to 50% in 2008, boards still ignored 50% of all precatory proposals supported by a majority of its shareholders).
shareholders the power to make rules-of-the-game decisions”100 and argued that shareholders should be given the power to adopt changes in the certificate of incorporation and to effect reincorporations “unilaterally”, without the approval of the board of directors.101 Increasing shareholder power, according to Bebchuk, “would improve corporate governance and enhance shareholder value by addressing important agency problems that have long afflicted publicly traded companies.”102 Bebchuk thus wants to expand the set of proposals that can be introduced as binding, rather than merely as precatory, resolutions.

Opposing Bebchuk and favoring board control, Professor Steven Bainbridge argues that “vesting decision-making authority in a centralized nexus distinct from the shareholders (and all other constituents, for that matter) is what makes the large public corporation feasible.”103 Shareholders, according to Bainbridge “lack both the information and the incentives necessary to make sound decisions on either operational or policy questions.”104

The right to amend bylaws is, next to the right to elect directors, one of the few rights that shareholders can exercise unilaterally. Moreover, it is currently the only way for shareholders to change the governance rules without going through the board.105 So, from the perspective of shareholder rights advocates, bylaw amendments present a unique opportunity to be grasped, while, from the perspective of managerialists, they present a chink in the armor of board-centered governance. Bylaw amendments, one might think, are thus the battleground on which shareholders can assert their limited unilateral governance powers.

(c) The Reality

Curiously, however, shareholder proposals are usually precatory even if they do not have to be. A case in point is the AFSCME proposal. Separating the roles of CEO and Chairman is clearly within the purview of bylaw provisions (which establish these positions to start with) and

102 Id.
104 Id. At 21
105 Kahan & Rock, ___
a provision could easily be drafted. Moreover, JPMorgan does not impose any super-majority voting requirements for shareholder bylaw amendments.\textsuperscript{106}

The AFSCME proposal is not unusual. Almost all shareholder proposals dealing with the separation of CEO and Chairman – the single most popular governance proposal in the 2012 season\textsuperscript{107,108} -- are introduced as precatory resolutions.\textsuperscript{109} And so are shareholder proposals on a variety of other topics that could be implemented through bylaw amendments: proposals on confidential voting; proposals on director qualifications; proposals to staff certain committees with independent directors; proposals to allow shareholders to recover costs from proxy contests; proposals to repeal exclusive forum bylaws; and proposals on majority voting for directors.\textsuperscript{110} Rule 14a-8 proposals for mandatory bylaw amendments are extraordinarily rare.\textsuperscript{111} Why, with so much at stake, would shareholders opt for a precatory rather than a mandatory provision?

5. \textbf{Supermajority Shareholder Proposals}

(a) The Issue

Under state law, certificates of incorporation can generally be amended if the board recommends an amendment and the amendment is approved by the vote of a majority of the outstanding shares.\textsuperscript{112} As noted above, bylaws can be amended by a vote of a majority of shares.\textsuperscript{113} State law, however, permits companies to impose higher voting thresholds for


\textsuperscript{107} See Georgeson, supra note __, at 18.

\textsuperscript{108} Over the five-year period 2008-2012, of the 151 shareholder proposals to have an independent board chairman or to separate the roles of CEO and chairman, all but eight (94.70\%) of these proposals were precatory. See, GEORGESON, ANNUAL CORPORATE GOVERNANCE REVIEW (2008-2012).

\textsuperscript{109} Of the 22 proposals for confidential voting between 1998 and 2002, none were precatory. Of the 14 proposals regarding director qualifications from 2010 to 2012, all but three were precatory. Of the 151 shareholder proposals regarding majority voting for directors over the five-year period 2008-2012, all but two were precatory. Of the 19 proposals from 1998 to 2008 to staff certain committees with independent directors, only one was not precatory. See GEORGESON, ANNUAL CORPORATE GOVERNANCE REVIEW (1998-2012).

\textsuperscript{110} Out of the 1561 shareholder proposals tracked by Georgeson and voted on over the five-year period 2008-2012, only 46 proposals (2.95\% of all proposals) were binding bylaw amendments. GEORGESON, ANNUAL CORPORATE GOVERNANCE REVIEW 12, 20 (2012).

\textsuperscript{111} Del. Code Ann. tit. 8, § 242(b)(1).

\textsuperscript{112} Del. Code Ann. tit. 8, § 109(a).
shareholder approval.\textsuperscript{114} Some companies have availed themselves of this opportunity and provided that some provisions in the charter or the by-laws can be changed only with the vote of a super-majority of shares.

Shareholder activists have recently started to focus on these super-majority provisions. Lately, Standard and Poor 1500 companies have received between 10 to 20 such proposals a year, making elimination of super-majority voting requirement one of the most common corporate governance proposals.\textsuperscript{115} Proposals to eliminate super-majority voting are also amongst the ones that obtain the highest level of shareholder support.\textsuperscript{116}

(b) The Rhetoric

Shareholder activists view elimination of super-majority provisions as highly important. As recently argued in a supporting statement,

Corporate governance procedures and practices, and the level of accountability they impose, are closely related to financial performance. Shareowners are willing to pay a premium for shares of corporations that have excellent corporate governance. Supermajority voting requirements have been found to be one of six entrenching mechanisms that are negatively related with company performance. … If our Company were to remove required supermajority, it would be a strong statement that our Company is committed to good corporate governance and its long-term financial performance.\textsuperscript{117}

\textsuperscript{114} Del. Code Ann. tit. 8, § 102(b)(4).
\textsuperscript{115} See, GEORGESON, ANNUAL CORPORATE GOVERNANCE REVIEW (2008-2012). Elimination or reduction of super-majority voting provisions has been one of the 10 most common corporate governance proposals over the five-year period 2008-2012. In 2012, it was the 6\textsuperscript{th} most common proposal. Since many companies do not have any supermajority requirements than can be eliminated, the incidence of such proposals on the relevant subset of companies with such requirements is much higher.
\textsuperscript{116} \textit{Id.} In the five-year period 2008-2012, proposals to eliminate or reduce super-majority voting provisions were within the top three most supported proposals. For example, in 2012, these proposals, on average, received 69\% of shareholder approval.
\textsuperscript{117} http://www.sec.gov/Archives/edgar/data/915389/000095012311028540/g25811ddef14a.htm#G258811146
Supporters of such provisions, including companies faced with such proposals, are equally certain that supermajority provisions are necessary to protect minority shareholders against coercion and oppression by the majority.118

(c) The Reality

Whether super-majority voting requirements matter depends on what substantive provisions are entrenched by these requirements. In some instances, charters impose super-majority requirement on shareholders’ ability to remove directors without cause or to amend the bylaws or entrench staggered boards. These provisions could have a plausible impact on corporate governance because staggered boards can impede a hostile takeover and shareholders may seek bylaw amendments to establish proxy access, separate the positions of Chairman of the Board and CEO, and the like.

In other cases, however, some or all of the substantive provisions protected by a super-majority vote against amendment are of extremely remote relevance. Consider, for example Eastman Chemical Company where a shareholder proposal to eliminate super-majority vote requirements was received in the 2011 proxy season. At the time, the company’s charter required a 2/3 super-majority for shareholders to remove directors for cause and to amend the bylaws. For-cause removals at public companies are virtually unheard of and the likelihood that anyone would seek to remove any director for cause and receive a majority, but less than 2/3 shareholder support is extremely remote.

Perhaps the Eastman Chemical proposal was exclusively targeted at the super-majority requirement for bylaws amendments and just painted with a broad brush. But then consider Ecolab Inc., which also received a shareholder proposal to eliminate super-majority vote

118 For example, in recommending shareholders vote against a proposal to eliminate supermajority voting, the Kellogg Board stated that supermajority votes “[give] minority shareowners a greater voice in corporate structure and governance.” Kellogg Company, Definitive Proxy Statement (Schedule 14A), at 69 (Mar. 5, 2012) http://www.sec.gov/Archives/edgar/data/55067/000119312512095693/d287865dde14a.htm. See also Google Inc., Definitive Proxy Statement (Schedule 14A), at 68 (Apr. 20, 2011) http://www.sec.gov/Archives/edgar/data/1288776/00011931251103802/dde14a.htm (stating that the supermajority vote ensures that “fundamental changes to the organizational document of the company only occur with a broader consensus than a simple majority”), Paccar, Definitive Proxy Statement (Schedule 14A), at 41 (Mar. 10, 2011) http://www.sec.gov/Archives/edgar/data/75362/000095012311023929/v58490dde14a.htm (stating that the supermajority vote is “designed to protect all PACCAR shareholders against coercive takeover tactics”).
requirements in the 2011 proxy season. The substantive provision at issue was a “fair price” anti-takeover charter provision that required super-majority shareholder approval for certain “business combinations” with an “interested shareholder” unless the transaction was approved by a majority of the directors not affiliated with the interested shareholder or met certain "fair-price" and procedural requirements.119 Today, this sort of “fair price” provision is considered irrelevant because boards can use a poison pill to ward off any unwanted bidder, and, once a deal is agreed, the board will disable the provision by approving the combination. In the end, the shareholder resolution was approved, the board proposed the requisite amendment the following year, and the charter was amended to eliminate the provision.

A similar proposal the same year called for Sprint Nextel to remove any super-majority voting requirements in its charter and by-laws and opt-out of any such requirements imposed by state law (without specifying whether state law imposed such requirements).120 As in the case of Ecolab, the only super-majority voting requirements at issue appeared to be a “fair price” anti-takeover charter provision. The proposal passed and, the following year, the board recommended removing the fair price provision from the charter and, for good measure, opting out of the Kansas anti-takeover statute. Again, none of this mattered as Sprint Nextel has access to a poison pill. And since Sprint Nextel does not have a staggered board, any of these defenses - the pill, the anti-takeover statute, and the fair price charter provision – could be overcome by the simple (and, in hostile bids, common) ploy of seeking to replace the board while a hostile tender offer is pending.

Given the irrelevance of most super-majority provisions, and most shareholder proposals to eliminate those provisions, why do shareholders bring such proposals and why do managers resist?

**Part III: Understanding the gap between rhetoric and reality**

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119 http://www.sec.gov/Archives/edgar/data/31462/000104746911002336/a2202373zdef14a.htm#proposal7
120 http://www.sec.gov/Archives/edgar/data/101830/000095012311029718/l41834def14a.htm/#L41834147
With so much shareholder activism unrelated to any tangible benefit, why do shareholder activists engage in it and why do corporations and their defenders often resist it? In this Part, we will suggest several possible answers to this conundrum.

1. False Perceptions

One possible reason for symbolic activism is that the partisans wrongly believe that their activism has a direct substantive impact. Here we need to distinguish between leaders and foot soldiers.

Shareholder proposals are made by actors with a range of sophistication, from individual investors to governance professionals at institutional investors to hedge fund managers, with shareholder advisory firms, law firms and other sophisticated actors lobbying for and against. Some of these “initiators” may not have the legal sophistication to see, or may not want to expend the effort to determine, whether implementation of the proposal would matter. Thus, for example, some activists may believe that proxy access would have enabled shareholders to get board representation at little effort and expense. Or they may not have checked the details of a company’s charter provision to determine whether a super-majority vote requirement relate to any provision that was significant.

Rank and file individual and smaller institutional investors – who are presented with proposals made by others – may well be confused about the importance and effects of issues like poison pill proposals, proxy access, majority voting, and so forth. Like ordinary voters in any election, the rank and file shareholders have limited knowledge and minimal incentives to delve deeply into issues or to hire sophisticated advisors. It is not implausible to imagine that small institutional investors who received an ISS recommendation to oppose poison pills not approved by shareholders might have thought that doing so would preclude companies from adopting a poison pill in response to a hostile bid.

Consistent with this possibility, companies -- who have access to sophisticated legal advice and will bother to check the facts – sometimes do not resist certain activist campaigns. Thus many companies do not bother to renew their poison pill in order not to incur the activists’
wrath, because there is little point in doing so. But while it is possible that some activists are simply uninformed, this is unlikely to be the full story. The key actors who determine the outcome of most campaigns are sophisticated and have access to well-informed advisors. It is inconceivable that large institutional investors, hedge funds, and proxy advisors are simply confused about, for example, the legal impact of a company not renewing its poison pill. Thus, when ISS instituted a policy to oppose most poison pills that were not approved by shareholders, or when Fidelity developed its proxy guidelines opposing most such pills, we do not believe that ISS and Fidelity believed that the company would be barred from implementing a pill if it became subject to the hostile bid. Something more must be going on.

2. “Public Interest” explanations: change is hard and the battle is long

(a) Principles Matter

Suppose that everyone understands the gap between rhetoric and reality in shareholder activism. It is still possible that the partisans nevertheless choose to wage a battle as a matter of “principle.” In fact, many of the proxy guidelines published by mutual funds sound as if principles matter. Thus, for example, Fidelity will generally withhold its vote on all incumbent directors – regardless of other factors – if the board adopts a poison pill without shareholder approval, unless the pill meets certain narrow criteria. The New York State Common

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121 Katz & McIntosh, supra note __, at 5 (“when confronted with shareholder pressure, there is no need for a board to incur negative publicity by renewing an unpopular poison pill … A company is better served when the board eschews a fight on this issue and simply retains the flexibility to adopt an effective rights plan in response to a takeover threat.”)

122 See Wachtell, Lipton, Rosen & Katz, Key Issues for Directors, Dec. 6, 2006 (recommending that boards accommodate proposals to institute majority voting).

123 Weil Gotshal, RiskMatrics/ISS Issues Policy Updates for 2010 Proxy Season, Nov. 23, 2009, at 2, available at www.weil.com/files/upload/briefing_sec_cg_2009_nov.odf (stating that ISS will “recommend a negative vote with respect to all continuing directors” where the board has adopted, renewed, changed or maintained a pill “without shareholder approval.”)

124 Fidelity Investments, Fidelity Funds’ Proxy Voting Guidelines, Nov. 2012 at III.A.1., available at http://personal.fidelity.com/myfidelity/InsideFidelity/InvestExpertise/governance.shtml (stating Fidelity will “generally withhold authority for the election of all directors or directors on responsible committees” if a poison pill was introduced, extended or adopted “without shareholder approval”)

125 Id. Examples of these narrow criteria are if the poison pill includes a “sunset provision of less than five years” or a “permitted bid feature,” if the pill is “linked to a business strategy that will result in greater value for the shareholders” or if “shareholder approval is required to reinstate the poison pill upon expiration.”
Retirement Fund will support proposals to eliminate supermajority requirements – without apparent regard to what they pertain to -- because supermajority provisions “can be used to defeat corporate democracy.”\textsuperscript{126}

How might principles matter? High profile battles over principles may have significant educational value. In the shift in U.S. boardrooms from a managerial conception of the role of the board to a more “shareholder-centric” view, these battles almost certainly were important in reorienting directors’ understanding of their roles. Moreover, for those directors who believe that their role is to further shareholder interests, evidence from activist battles may inform their decision-making.

(b) Proxy Battles

A further possibility is that these battles are actually a fight about a different issue. Perhaps battles over principles, even when they make no practical difference, matter, at least when both sides agree that they do. There are several ways in which this may work.

First, prevailing on a matter of “principle” may nevertheless have implications for the future. For one, it can be a show of strength, of the activist’s ability (or the activists’ abilities) to mobilize shareholder support, garner votes, and obtain public support. It signals to the people on the other side, mostly executives and outside directors, but perhaps also politicians and regulators: “Do not cross me, or else.” By the same token, once a battle has commenced, not prevailing or showing weakness signals to the other side that the activist can be safely ignored. The outcome of the contest may be interpreted to mean “shareholder forces are ascendant” or “management is still in control.”

This is clearly how the press reports on the results. Thus, for example, the Court of Appeals ruling invalidating proxy access was described as “striking a blow to the ‘shareholder rights’ movement”\textsuperscript{127} and the failure to separate the CEO and Chairman position at J.P. Morgan

induced BusinessWeek to predict “[n]ow that they’ve picked the fight with the biggest kid on the block – i.e., JPMorgan and Jamie – and lost it, other people are going to say, ‘How powerful are you guys?’” 128

Indeed, from this perspective, the partisans may be aware that the direct stakes are low and may even see an advantage in waging battles over issues that do not matter. Battles without a tangible effect mean that the collateral damage inflicted is low. What better way, for example, to show one’s power than to push companies not to renew their poison pills or to remove essentially meaningless provisions for supermajority voting. Since the impact is symbolic, success can do little direct harm. Much safer to stick to symbolic matters rather than, for example, enact mandatory bylaw amendments that may be hard to reverse.

Moreover, the risks to activists from being wrong are much reduced in battles over principle. In 2007, shareholders rejected Carl Icahn’s $37.25 per share offer for Lear Corporation, an automobile parts manufacturer, after ISS and Glass Lewis both recommended voting against. 129 Two years later, Lear Corp. filed for bankruptcy. 130 A few more recommendations like this could lead investors to stop following ISS and Glass Lewis. 131

It also makes sense that the issues chosen for symbolic activism will have some mass appeal. Fighting for shareholder democracy, majority rule, opening access to the ballot may lead to increased support and thus contribute to the goal: winning. Moreover, it is likely to garner favorable press attention.

The ultimate objective, according to this explanation, goes beyond the explicit issue over which the battle is waged. Rather, the battles exert pressure on directors to pay more attention to shareholder concerns more broadly. If activists can prevail on a shareholder proposal, they are

128 Nick Summers, Jamie Dimon Wins Big in JPMorgan Shareholder Vote, BUSINESSWEEK (May 21, 2013) http://www.businessweek.com/articles/2013-05-21/jamie-dimon-wins-big-in-jpmorgan-shareholder-vote. When referring to shareholder democracy groups’ failed attempt to bar Dimon from serving as chairman and CEO, the article reported “[n]ow that they’ve picked the fight with the biggest kid on the block – i.e., JPMorgan and Jamie – and lost it, other people are going to say, ‘How powerful are you guys?’”

129 July 16, 2007 USA Today Lear Shareholders reject $2.9 B Icahn Deal.

130 Reuters, July 7, 2009 Auto parts maker Lear Cop files for bankruptcy.

131 Given this risk, it should be unsurprising that, after raising questions about the controversial Dell going-private offer but failing to attract competing bids, ISS, Egan-Jones and Glass Lewis all ultimately recommended shareholder approval. Shira Ovide, ISS, Two Others Recommend Dell Buyout, WSJ July 9, 2013 http://online.wsj.com/article/SB10001424127887323823004578593230519805900.html?mod=WSJ_hps_sections_business.
more likely to be able to prevail in other battles that matter more. For larger shareholders, being taken seriously when it matters is extremely important. It assures that senior management will at least listen to you when you have doubts over the company’s business strategy. It induces the lead director to take the telephone call from the institutional investor when the company is facing an actual hostile bid, when the board is deliberating whether to fire the CEO, when the board is looking to add some independent directors, or when management has made a buyout offer. It gets you access to the head of the compensation committee when you want to push for greater performance sensitivity in the CEO’s pay.

More generally, the battles may be part of a broader public policy initiative to change law and regulation in a direction that gives shareholders more power. Having prevailed in these symbolic battles, activists can more credibly lobby the SEC and Congress to increase shareholder power further. “The shareholders overwhelming support increasing shareholder power,” activists can argue, “look at the support for these shareholder proposals relating to X, Y and Z.”

(c) The Slippery Slope

Another possibility is that partisans view corporate governance politics as a multi-year, multi-engagement process, so that the first battle in a campaign may take on outsize importance. Consider, for example, the battle over the SEC’s “proxy access” initiative. As we have argued elsewhere, the 3 percent/3 year threshold for access to the corporate proxy statement meant that the SEC’s initiative would likely have had minimal effects: shareholders who might have used proxy access would not have qualified; while shareholders who would have qualified would likely not have been interested or would have been unwilling to accept the limitations that accompanied it.\(^{132}\)

So why was there a hard fought battle? One plausible explanation is that partisans on both sides hoped (or feared) that the proposed (and adopted) proxy access rules would just be the first step. If enacted and held valid, and not used, activists could have returned to the SEC to argue that the thresholds should be lowered, the limitations relaxed, and so forth. Better and easier to fight it at the outset, defenders of management might have thought, than to have to fight constant battles against incremental expansion.

\(^{132}\) Kahan & Rock, supra note __.
3. **“Public Choice” Explanations: It’s the Activists, Stupid**

A somewhat related, and perhaps complementary (if not complimentary), possibility is that professional activists, at least those who are governance professionals at institutional investors or who work at ISS and Glass Lewis, are aware of the large gap between rhetoric and reality in their campaigns, but pursue activism for its own (or rather their own) sake. What keeps activists busy – and employed -- is activism.

Take, for example, ISS, the leading proxy advisor. As part of its business, ISS provides voting advice to its clients on all issues that shareholders are asked to vote on. It may not be conducive to ISS’s business were its advice on shareholder proposals to redeem a pill a dismissive “This issue is of no practical significance. It really does not matter how you vote.” Nor would it behoove ISS to proclaim that the voting rules on the most common ballot question for shareholders – whether to vote for nominees to the board or to withhold authority – is not very important. If none of this matters, why would investors pay ISS for its voting advice? Surely, the price ISS could charge would be higher if shareholders vote on issues that matter. Governance professionals working directly for large institutional investors face similar incentives.

Corporate lawyers advising boards may likewise have an incentive to overstate the importance of some of the issues. They can enhance their business by privately advising companies on how to respond to activist campaigns - and advice to do something tends to generate more business than advice to do nothing. They can also enhance their reputations as fervent defenders of managerial power by publicly opposing the activist efforts. Leading corporate lawyers may well have been aware that the SEC’s proposals on proxy access were unlikely to pose a serious threat, but they may still have opposed it in editorials and comment letters to impress their clients.

4. **Symbols and Myths: What would Thurman Arnold say?**

The indirect “public interest” explanations, combined with the “public choice” perspective go some way towards explaining why these battles continue, even when the direct stakes seem trivial to a dispassionate observer. But more seems to be at stake than appears in
any of these explanations. These battles can feel like they involve issues that are genuinely important matters of national import. Could Arnold account for that feeling?

How might a Thurman Arnold describe our current “Folklore of Corporate Governance”? What is the conflict that corporate governance reform might be understood to provide a “ritual” response to? A moment’s reflection suggests that our myths have not changed appreciably since the 19th century rise of the great industrial corporations. Now, as then, we need to believe that, in even -- and especially -- the largest corporations, there are shareholders who collectively own the corporation and control it. Because shareholders exercise control over the managers, perhaps mediated through markets, it is acceptable that a small group of managers control huge concentrations of capital and get paid princely sums for doing so.

We struggle with just the sort of gaping hole that Arnold found so obvious. A Thurman Arnold would find it laughable to claim that this picture accurately describes the large, publicly held corporations that are the focus of corporate governance reform. First, as scholarship on institutional investors has described, shares are held by intermediaries and managed by agents whose incentives at best roughly track those of the ultimate beneficiaries.133 And, over the last 40 years, ownership by institutional investors has steadily increased from 15% in 1965 to around 50%.134 There are essentially no shareholders of the sort that the myth hypothesizes. Second, while various sorts of intermediaries do exercise some direct and indirect control over managers of large firms,135 it does not remotely approach the degree assumed by the mythical picture of a limited number of actual individual shareholders who elect directors to manage their property. Finally, when economic actors actually emerge who might play the role laid out for shareholders – think of hedge funds – a reaction against them immediately appears.136

134 Kahan and Rock, Embattled CEOs, supra note ___ at 995-97.
135 Kahan & Rock, Embattled CEOs, supra note ___.
136 See Martin Lipton, Bite the Apple; Poison the Apple; Paralyze the Company; Wreck the Economy, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE AND FINANCIAL REGULATION (Feb. 26, 2013 09:22AM) https://blogs.law.harvard.edu/corpgov/2013/02/26/bite-the-apple-poison-the-apple-paralyze-the-company-wreck-the-economy/ (stating that shareholder voting power is being “harnessed by a gaggle of activist hedge funds whole troll through SEC filings . . . looking for . . . short-term profit without regard to . . . the company’s long-term prospects”), Activist Investors: Let’s Do It My Way, ECONOMIST, May 25, 2013, available at 2013 WLNR 12729847 (stating that hedge fund activists “pester firms for a quick return of cash to shareholders”).
Yet, as Arnold would be quick to point out, because the myth of American corporate governance conflicts with the reality of large publicly owned corporations, and because large concentrations of capital are necessary for many business entities operating in world product and capital markets, “it was inevitable that a ceremony should be evolved which reconciled current mental pictures of what men thought society ought to be with reality.”\textsuperscript{137} Just as “it became necessary to develop a procedure which constantly attacked bigness on rational legal and economic ground, and at the same time never really interfered with combinations,”\textsuperscript{138} so, too, it became necessary to develop a procedure which constantly attacked “managerial agency costs” or the “separation of ownership and control” on rational legal and economic grounds, and at the same time never really interfered with a separation that was a practical necessity when economies of scale required massive concentrations of capital.\textsuperscript{139}

Like the “curse of bigness,” the beauty of viewing “the agency cost problem” as the core problem of corporate governance is that every time there is a crisis and a call for regulation, one can respond, “if only managers’ interests were better aligned with those of the shareholders” and enact measures that claim to improve that alignment. After the dot com bubble burst, we had Sarbanes-Oxley.\textsuperscript{140} After the crash of 2008, we had Dodd-Frank.\textsuperscript{141} The SEC even managed to justify the rules on proxy access by reference to the financial crisis.\textsuperscript{142}

But, at the same time as Arnold would find the claims of corporate accountability laughable, he would save particularly sharp criticism for those reformers who would make us live up to our institutional creed by actually empowering individual shareholders to control managers! That, he would undoubtedly argue, is the road to ruin.

\textsuperscript{137} Folklore at 207.

\textsuperscript{138} Folklore at 207.

\textsuperscript{139} The history of the battle for “shareholder democracy,” recounted in Dalia Tsuk Mitchell, Shareholders as Proxies: The Contours of Shareholder Democracy, 63 Wash. & Lee L. Rev. 1503 (2006), provides additional detail on the almost endless variations on a theme.


\textsuperscript{142} See \url{http://www.sec.gov/rules/final/2010/33-9136.pdf} at 7 (“We recognized at that time that the financial crisis that the nation and markets had experienced heightened the serious concerns of many shareholders about the accountability and responsiveness of some companies and boards of directors to shareholder interests, and that these concerns had resulted in a loss of investor confidence. These concerns also led to questions about whether boards were exercising appropriate oversight of management, whether boards were appropriately focused on shareholder interests, and whether boards need to be more accountable for their decisions regarding issues such as compensation structures and risk management.”)
Indeed, from an Arnold perspective, what we most need, and have of course already developed, is a ritual that allows us to live with the contradictions, while practical non-ideological men figure out how to make institutions serve social needs. For Arnold, “the making of quack corporate governance,” is just the latest version of a process that traces back into the Middle Ages and beyond, that should as easily be cynically celebrated as sincerely condemned.

From this perspective, the focus of attention is almost but not entirely arbitrary. The best issues to fight about are not those with the greatest effect on firm value but, rather, those that invoke core commitments. It hardly seems coincidental that the hardest fought battles involve issues that revolve around “shareholder democracy”: proxy access, majority voting, elimination of supermajority requirements. These issues immediately tap into broader themes and commitments, however disanalogous political and shareholder voting are. The battles over poison pills are likewise cast in “democratic” terms: a poison pill is bad because it prevents shareholders from deciding for themselves whether to accept a tender offer. Populist themes are nearly as popular as “shareholder democracy,” with anything to do with executive compensation a reliable crowd-pleaser: say on pay, shareholder approval of incentive compensation, anti-golden parachute proposals, etc. With these sorts of issues, it is immediately obvious which side is which, an absolute necessity in any Kabuki play.

Part IV: Implications

Our account of the gap between rhetoric and reality in shareholder activism has several implications for the corporate governance debate.

1. Chicken Little

The most direct implication is to take the rhetoric used by activists on all sides with a large pinch of salt. Despite protestations to the contrary, many issues that profess to be at the...
foreground of shareholder activist campaigns and managerialists’ counter-campaigns do not have such weighty implications. Fundamental precepts of shareholder democracy are not, in fact, at stake and it generally is not very likely that any reform movement will generate “profound effects,” be “groundbreaking,” or “wreak havoc.” Whether activist campaigns succeed or fail, the sky will not fall. Chicken Little can relax.

2. Activists Just Want to Have Fun

The focus by shareholder activists on core commitments to shareholder democracy and on issues capable of rallying mass support has costs. First, it can divert attention away from more significant changes that will provoke more significant opposition. Second, it can divert attention away important technical issues that are hard to fit into the standard shareholders versus managers frame.

Consider, for example, the multi-year battle on proxy access that claimed to be about reducing the costs of running a competing slate of candidates. Put aside the fact that after multiple SEC proposals and years of analysis, the SEC was not able to come up with a proposal that survived a challenge for not being “arbitrary and capricious.” Even if the SEC rule had been upheld, it would have had a minimal impact of corporate governance: only few shareholders would have qualified to nominate shareholders under the proxy access regime and most of the shareholders who would have qualified have shown no appetite in the past of getting involved in more hard-core forms of governance activism. More importantly, however, the proxy access proposal failed in the basic goal of substantially reducing the costs of proxy contests. While the rule would have made it easier to get a nominee on the ballot and would have reduced the costs of collecting ballots, the bulk of expenditures incurred in actual proxy contest– campaign expenses – would not have been affected by the rule.

While activists were preoccupied with proxy access, they were oddly silent on two other issues that actually can have significant effects. The first is discretionary broker voting in

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145 See supra note __.
146 See supra note __.
147 See supra note __.
148 Business Roundtable v. SEC, 647 F.3d at 1156.
149 Kahan & Rock, supra note __, at 1375-83.
150 Id. at 1383-94.
director elections. Historically, the New York Stock Exchange had regarded uncontested
director elections – that is, elections where there is only one slate of nominees – as routine, even
when some shareholders waged an active campaign to convince other shareholders to “withhold”
their votes from certain nominees. On routine issues, brokers are permitted to cast the votes of
uninstructed shares. As a result, brokers could vote shares of any holders for which no specific
instructions were received in favor of the board nominees. According to some estimates,
uninstructed shares may account for 19% of the votes cast at annual meetings.

With the rise of “withhold” votes, even uncontested elections became non-routine. Thus,
in October 2006, the NYSE proposed to amend Rule 452 governing broker votes to redefine all
director elections as non-routine. The proposed change required SEC approval to become
effective. If there ever was a pretty simple decision, one would have thought that this was it.
What reason could the SEC possibly assert for blocking the NYSE from adopting a rule that
takes voting authority away from brokers who lack any economic interest in the underlying
shares? Yet, it took the SEC over two years to solicit comments on the NYSE proposal and
almost three years to approve it. Activists, for the most part, did not exert significant pressure
on the SEC to move sooner and faster.155

The second issue is reimbursement of proxy contest expenses. At the same time as
Delaware clarified that a proxy access regime could be adopted through bylaws, it also clarified
that bylaws could provide that the company reimburse reasonable expenses incurred by proxy
challengers, either outright or subject to conditions (such as achieving a certain threshold of
success). Expense reimbursement could potentially have a much stronger impact on corporate
contests than proxy access because it would cover a much greater portion of the relevant proxy
contest expenses. Yet activists have done virtually nothing on the expense reimbursement front:
they have not developed model provisions for companies to enact or shareholders to propose,

151 Kahan & Rock, supra note __ at 1016.
152 See SEC Hears Testimony on Broker Votes, May 25, 2007, at http://blog.riskmetrics.com/2007/05/ (attributing this figure to Broadridge Financial). This may be an over-estimate. See Kahan & Rock, supra note __, at 1016-17.
154 Kahan & Rock, supra note __ at 1017.
156 DGCL, Section 113.
they have not rallied support for an expense reimbursement regime, they have not submitted precatory resolutions or mandatory proposals in meaningful numbers, they have not pushed for any legislative or regulatory actions.

In some ways, the fact that activists ignored discretionary broker voting and expense reimbursement is odd. These issues, like others that became the focus of activist attention, relate to shareholder democracy. Perhaps activists thought that they are less sexy than proxy access. Perhaps they worried that success would be elusive because managers would spare no expense in opposition. Or, perhaps, they were just too busy with the campaign du jour to take on another issue at the same time.

More technical issues that cannot be neatly cast as “pro-management” or “pro-shareholder” and do not serve this symbolic function receive even less attention. The SEC’s “proxy plumbing” concept release has received very little attention from the activist community, even though it addresses fundamental flaws in the infrastructure of shareholder voting. It is pretty difficult to rouse an “audience to a high pitch of indignation” over complications created by a proxy voting system combined with multiple layers of custodial ownership that arise out of an old decision to immobilize shares rather than dematerializing them. Even technical issues like streamlining the share voting process, although more tightly aligned with hot button issues like “shareholder democracy,” fail to generate much attention.

3. Shades of Grey

A proper understanding of the nature of the governance debates and its exaggerated rhetoric should also imbue us with some skepticism about who are the “good guys” and the “bad guys.” Shareholder activists and managers and their defenders all have more complex motivations than maximizing firm value or protecting privileges. To be sure, managers are agents and are subject to agency costs: what benefits them is not perfectly aligned with what

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157 Georgeson lists no single proposal on reimbursement of expenses in its overview of 2012 proposals. See Georgeson, supra note__, at__. For the 10-year period 2003-2012 there have been only 12 proposals to allow shareholders to recover proxy contest costs.
158 confirm
160 Folklore at X.
161 See, e.g., Kahan and Rock, Hanging Chads.
benefits shareholders. But shareholder activists – whether they are governance professionals at institutional investors, union or public employee pension funds, individual shareholders who specialize is submitting 14a-8 proposals, or academics advocating greater shareholder powers – are often agents as well and frequently have incentives that are not aligned with those of shareholders at large. Individual shareholders who hold substantial stakes but no managerial role and are plausibly motivated to maximize the value of their portfolio are largely absent from both sides of the issues.

Rather than epic battles between the forces of good and evil, governance debates thus involve disputes between different shades of grey. Neither side is entirely free from self-interest, and neither side has a monopoly on valid arguments. A symbolic victory by shareholder activists may have both good and bad consequences, and the balance of consequences may differ from firm to firm.

Take, for example, the wholesale shift from plurality voting to majority voting in large firms. While good arguments can be made in favor of majority voting, both as a matter of principle or from a pragmatic perspective, we are not convinced that the rapid and widespread adoption of majority voting by large firms was warranted.\(^{162}\) We are also not sure why firms outside the Standard & Poor’s 500 lag behind in their adoption of majority voting.\(^ {163}\) Is it because activists have arrived at the conclusion that the governance regime for smaller firms should differ from the one for large ones or is it because there is less glamor is inducing governance changes in smaller firms?

4. The Best of All Possible Worlds?

Finally, taking the perspective of Thurman Arnold, one may observe all the battles and conclude that we live, if not in the best of all possible worlds, then at least in a pretty good one. Despite the back and forth, corporate governance in the U.S. is characterized by a high degree of stability and slow paced, gradual change. Because we have created the illusion of shareholder control – maintained by the symbolic, and largely harmless, disputes we have discussed in this article – the current system of corporate governance enjoys widespread support. Shareholder

\(^{162}\) See supra TAN.

\(^{163}\) See supra TAN; see also Lucian A. Bebchuk & Scott Hirst, *Private Ordering and the Proxy Access Debate*, 65 BUS. LAW 329, 343 (2010) (as of September 2009 only 12% of the 5,390 firms outside of the S&P 500 have majority voting).
activism, rather than undermining the legitimacy of the current system, serves a legitimating function showing that reform for the better is possible and that shareholders have power.

In truth, however, the actual power in corporations is wielded by a limited set of actors who are not the beneficial holders of the equity interests. This set may be somewhat wider than it was in Arnold’s time, but is dominated by the establishment. First and foremost, the CEO remains the dominant force, if less so than 20 years ago.\textsuperscript{164} Other forces include outside directors, major institutional investors, and activist hedge funds. These actors are involved in setting up the incentive structure for CEOs and occasionally get involved when there is a crisis or a vacancy to be filled. On day-to-day matters, however, the CEO calls most of the shots, and is left to do so as long as she does as reasonably good job in managing the corporation.

Waging symbolic battles, some of which may be won, may thus dull the public’s desire for actual, fundamental change. On the issues that matter, we are largely in equilibrium. As a result of having created the myth of shareholder control, we can politically accept a system that is economically beneficial. Thurmond Arnold, ultimately a member of the establishment, would smile at Vanity’s Fair, appreciating shareholder activism’s spectacle, glitter and performance, at the same time as he would turn his attention to seeking practical non-ideological solutions to practical non-ideological problems.

**Conclusion**

The politics of corporate governance reform shares much with politics more generally. In both, there is a persistent gap between rhetoric and reality. In both, that gap may reflect the difficulty of change, the pursuit of a long-term strategy, the ignorance and confusion of participants, and rent seeking by interest groups of one sort or another. But, beyond these conventional explanations, we should be alive to the possibility that corporate governance politics, like politics more generally, may serve a “mythological” or “symbolic” function separate and apart from these more instrumental and practical uses.

*The Folklore of Capitalism*, Thurman Arnold’s ironic masterpiece, can serve as a useful corrective to the dominant modes of analysis. Focused as it ultimately is on the regulation of

\textsuperscript{164} Kahan & Rock, Embattled CEOs, supra note __.
business, it provides a refreshing perspective on current controversies that, at their heart, are not so different from the battles over the New Deal that animated the analysis. Arnold’s analysis provides three useful “takeaways.” First, we ignore the “ritual” function of corporate governance politics and law at our peril. Second, well-meaning reformers who insist that we live up to our ideals can cause real harm. No real world institutions can survive that test.

Finally, Arnold reminds us that, as essential as myths may be, we must guard against allowing them to confuse us in analyzing real world problems. Here, his warnings of the mischief that can be caused by taking the concept of “corporate personality” too seriously, discussed above, provide a cautionary reminder. It does not take much imagination to guess how Arnold would have reacted to the use of “corporate personality” in the line of United States Supreme Court cases culminating in Citizens United v. FEC.165 In summarizing that history, the majority’s opinion stated that:

Under the rationale of these precedents, political speech does not lose First Amendment protection "simply because its source is a corporation." Bellotti, supra, at 784, 98 S. Ct. 1407, 55 L. Ed. 2d 707; see Pacific Gas & Elec. Co. v. Public Util. Comm'n of Cal., 475 U.S. 1, 8, 106 S. Ct. 903, 89 L. Ed. 2d 1 (1986) (plurality opinion) ("The identity of the speaker is not decisive in determining whether speech is protected. Corporations and other associations, like individuals, contribute to the 'discussion, debate, and the dissemination of information and ideas' that the First Amendment seeks to foster" (quoting Bellotti, 435 U.S., at 783, 98 S. Ct. 1407, 55 L. Ed. 2d 707)).

The Court has thus rejected the argument that political speech of corporations or other associations should be treated differently under the First Amendment simply because such associations are not "natural persons." Id., at 776, 98 S. Ct. 1407, 55 L. Ed. 2d 707; see id., at 780, n. 16, 98 S. Ct. 1407, 55 L. Ed. 2d 707. Cf. id., at 828, 98 S. Ct. 1407, 55 L. Ed. 2d 707 (Rehnquist, J., dissenting).

There are a variety of arguments that can be made for and against the regulation of corporate campaign expenditures, but the “corporate personality” of corporations is not one of them. Arnold would surely argue that we continue to be confused by our myths.