

Food for Thought

July 2009

Dissatisfied shareholders – What recourse do they have?

Food for Thought is our way of sharing interesting concepts on corporate leadership and management with others who might find it useful. The thoughts offered are intended to be controversial and thought provoking. They always follow our motto of helping develop logical leadership.

What recourse do activist shareholders of public companies have when they are dissatisfied with their board? Can they take them to court? Citing the business judgment rule, the courts have been reluctant to second guess the boards' decisions as long as they have discharged their duty of loyalty and their duty of care. The courts have maintained that shareholders' recourse is to elect a different board. The shareholders have complained that with the company's proxy controlled by the incumbent board, it is difficult, if not impossible, to oust or replace sitting directors. In turn, shareholders have sought access to the company's proxy. The recent upheaval in corporate America, and the resulting pressure for reform on Congress, has resulted in a recent proposal by SEC to provide proxy access to "significant" shareholders. Directors rebut that providing proxy access to shareholders will result in nominations representing singular agendas that are not in the interest of the larger base of shareholders. With that as the backdrop, we offer a provocative, and likely controversial, idea.

What if the SEC required corporate boards of public companies to nominate a slate of candidates in excess of the number of slots to be filled, say in excess by at least 25%, failing which the boards must accede proxy access to "significant" shareholders, as currently proposed by the SEC? Such a proposal would ensure that the shareholders have a real choice in the proxy, and yet allow the board to ensure that nominated candidates represent the broader interests of shareholders. The slated candidates will invariably provide an alternative to current directors. Activist shareholders can then remove sitting directors with whom they are dissatisfied, causing all directors to be more vigilant of the interests of shareholders. Of course, the company and the proxy statement would have to be restricted from using its resources and reach to advocate or advance the candidacy of any specific director.

Directors are likely to complain that such a beauty-contest-proxy will dissuade qualified candidates from serving as directors. They might also argue that the collegial atmosphere of the boardroom might be compromised with each director interested in their re-election. In our opinion, some turmoil and change in the boardroom, and some level instability of directors' tenure and re-election, might not be a bad thing.

We have received many responses to our Food for Thought mailings, asking if you can freely share and forward these thoughts. Indeed you can. All we ask is that a clear attribution to LogiStyle and our contact information are included. For the interested reader, we have archived some of our recent Food for Thought mailings at our website, and can be viewed at LogiStyle: Food for Thought Archive. As always, we welcome your comments. We hope your business is doing well. If we can be of any assistance please feel free to call – even, if just to chat.

Best Regards,

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