Hedge Fund Activism Seminar and Book Launch of Research Handbook on Shareholder Power

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Justice Ashley Black
Supreme Court of New South Wales

Hedge Fund Activism Seminar

The second wave of US hedge funds

Hedge fund activism has been described as “offensive” in character (not in a judgmental sense), so far as a hedge fund will identify an opportunity for activism and typically then acquires an interest to permit that activism. Relevant strategies of hedge fund activists include seeking management or financial change in target companies to create “value” from the balance sheet by selling non-core assets, undertaking buy-backs or paying a one-off dividend to shareholders; promoting a sale of the target as a going concern or by divesture of business operations; or promoting strategic changes or changes in target management. [1]

Professor Partnoy and Professor Thomas might fairly be described as pioneers in the scholarly analysis of hedge fund activism, a field which hedge funds entered in the late 1990s, with scholarly interest following from the mid-2000s.[2] Professors Partnoy and Thomas assembled a sample of hedge fund activism from 1999 to 2005 in a working paper published in 2005 which was plainly a significant contribution to the field, and both have also been involved in the development of subsequent and wider samples.[3]

In their recent paper, “The Second Wave of Hedge Fund Activism: The importance of reputation, clout and expertise” (August 2016), the authors (with Professor Krishnan) undertake a further analysis of activist interventions from 2008 to 2014, and find that “top investor hedge funds” (as defined) succeed, in part, by acquiring a reputation for “clout and expertise”. The authors have plainly undertaken a very substantial research exercise, drawing a significant amount of data from several sources, across a very large number of transactions. Their analysis extends beyond the global financial crisis, in 2008 and 2009, and a suggested reduction in hedge fund activity during that period, through to 2014.

This study provides detailed information as to recent developments in the US hedge fund industry, confirming, for example, the increase in size and

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[1] B R Cheffins and J Armour, “The Past, Present, and Future of Shareholder Activism by Hedge Funds” (2011) 37 *J Corp L* 51 at 60.
[2] F Partnoy, “US Hedge Fund Activism” in JG Hill & RS Thomas (eds), *Research Handbook on Shareholder Power*, 2015, p 99.
[3] A Brav et al, “Hedge Fund Activism, Corporate Governance and Firm Performance” (2008) 63 *Journal of Finance*, 1729–1775; L Bebchuk et al, “The Long-Term Effects of Hedge Fund Activism” (2015) 115 *Colum L Rev* 1085.

dispersal of the hedge fund industry in 2008–2014, with more participants and more targets, and indicating that no single US hedge fund activist has a substantial share of the market, and even those activists with the largest number of interventions have relatively small market shares. The study also finds positive returns for activists, following the announcement of their intervention, that appear to have existed pre-2007, continued through what they describe as the "second wave" of activism from 2008 to 2014. A similar analysis would not be possible in Australia, given the relative lack of corresponding interventions.

The study points to alternative measures of hedge fund success, including frequency of intervention, past success and "financial clout and expertise". The authors adopt an objective measure for identification of a category of "top investor hedge funds", in a manner that should avoid circularity, by reference to the size of their aggregate investments in the recent past. The authors note that this category of hedge funds has greater "financial clout", including from access to internal funding sources, and "expertise" in persuading target boards to agree to their demands, and have greater success in proxy fights and law suits relating to board representation changes. The study finds that interventions by "top investor hedge funds" (as defined) were associated with the highest returns after announcement, and that interventions by hedge fund activists that engaged most frequently were associated with relatively lower announcement period returns.

The study also finds that targets of activism by the "top investor hedge funds" (as defined) achieve greater returns on assets, sales revenue growth, and research and development spending, by comparison with the position after interventions by other hedge funds, and that the positive results achieved by "top investor hedge funds" are more likely to be due to operational improvements, resulting from board representation or monitoring of target management, rather than significant capital structure or dividend policy changes. That finding is significant, since there is an active debate in the United States as to the social utility of hedge fund activism. That conclusion would tend to support a view that hedge fund activism is generating "real" economic benefits, rather than, as some professional commentators have suggested both in the United States and Australia, short term financial gains through financial engineering, potentially at a long term cost.

The study also tests the correlation between the "most popular hedge funds" (which might in some circles seem to be a contradiction in terms) measured by number of media mentions, and investment returns, and finds that media popularity does not explain superior announcement period market reactions with as much statistical significance as the presence of "top investor hedge funds", as defined. That proposition might be simplified to the proposition that blowing one's own trumpet is not a guarantee of success.

The authors' observation that "top investor hedge funds" (as defined) target companies with significantly higher levels of takeover defences would have limited application in Australia, since Australian law and practice allows almost no room for takeover defences[4], and particularly does not allow mechanisms of the kind to which the authors refer, such as staggered boards, poison pills, golden parachutes, limits on constitutional amendments, or supermajority voting requirements for mergers.

Interestingly, the authors also find that there appears to be limited use of put and call options during this more recent period of activism, at least to the extent that that can be traced from publicly available information. The authors identify two possible explanations, the first that hedge funds could achieve their objectives by accumulating equity stakes through prime brokers, and the second, which is certainly plausible, that hedge funds were using equity and total return swaps instead of options and not publicly disclosing that information.

The study concludes in 2014, immediately before what they describe as "recent disruptions in the market for hedge fund activism, including substantial losses and failed interventions during 2015". It would be interesting to know whether any of the "top investor hedge funds" (as defined), were subject to the failures of 2015, if only because that would demonstrate a fact well known to entrepreneurs generally, namely that last year's spectacular success is, regrettably, sometimes followed by this year's equally spectacular failure.

The Australian experience

The Australian experience of economically driven shareholder activism[5] is more recent, and more limited, than the US experience.[6] There are still relatively few examples of economically driven shareholder activism in Australia.[7] The debate as to whether hedge fund activism is a "good thing" has also come to Australia and legal practitioners in the field have not been slow to take sides. In a presentation at the Court's Corporate Law

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[4] Takeovers Panel, *Guidance Note 12: Frustrating Action*.

[5] Economic activism can include objectives such as a change of the company's board, changes in business, operational management strategy, or initiatives to alter a company's balance sheet, capital structure or dividend policy.

[6] When I wrote a modest paper dealing with shareholder activism under the *Corporations Act* in 2006, the then examples of shareholder activism included activities of the Australian Wilderness Society, environmental activists, the Australian Manufacturing Workers' Union, controversies in respect of Goodman Fielder Ltd in 1994 and Coles Myer Ltd in 1995 and, of course, long-running controversies in respect of National Roads & Motorists Association: see A Black, "Shareholder Activism under the Corporations Act", *AMPLA Year Book* 2006, pp 234–254; P Ali et al, *Corporate Governance and Investment Fiduciaries,* 2003, p51.

[7] Examples include activist shareholders seeking to influence the business strategy and board composition of Fairfax in 2012 and Qantas Limited in 2013. An investor and fund manager requisitioned a shareholder meeting in 2013 to seek to force the sale of cross-shareholdings between Washington H Soul Pattinson & Co and Brickworks Limited. That shareholder meeting was cancelled when relief was not available to address tax issues in respect of the transaction. Proceedings were also brought in the Federal Court of Australia in respect of the matter. In 2014, a US based hedge fund, Lone Star Value Investors LP, unsuccessfully sought to replace the board of Antares Energy Limited an Australian listed company with US energy assets, by requisitioning a general meeting of the company to remove two directors and nominating five directors for election. Shareholders ultimately voted against that proposal. I will also refer to a case involving Molopo Energy Limited below.

Conference in 2014[8], David Friedlander, adopted a theme that is also taken up in US professional commentary, pointing to the attraction to activists of campaigns that can improve short-term share market value, by increasing the level of dividends or making one-off capital distributions, and identifying a potential risk to a company's longer term position from such campaigns. That proposition is hotly controversial in the US academic literature, with academic commentary having challenged the assertion that shareholder activism reduces middle and long term shareholder welfare.

Mechanisms of shareholder activism

I should briefly identify several avenues for shareholder activism in Australia, some of which are more and some less prospective than in the US. I will deal with this briefly since these matters are generally well understood.

First, an activist may seek to remove director(s) of a target under s 203D of the *Corporations Act*, which permits removal of a director of a public company by a simple majority of shareholders. For example, Lone Star acquired an interest of more than 5% of the shares in Antares between February and March 2014, and then requisitioned a general meeting of shareholders under s 249D of the *Corporations Act*, gave notice of resolutions to be moved at that meeting under s 203D of the *Act*, and required Antares to circulate a statement to shareholders relating to the resolutions proposed by Lone Star under s 249P of the *Act*.

Second, shareholders with at least 5% of the votes that may be cast at a general meeting may require directors to call and arrange to hold a general meeting, within 21 days after the request is given, and at the company's expense.[9] Environmental activists have previously relied on this provision.[10] If directors fail to convene a meeting within 21 days of a request being given to the company, shareholders who hold more than 50% of the votes of the requisitioning shareholders may call and arrange to hold the meeting themselves at the company's expense and the company may recover that expense from the directors in an appropriate case.[11] Shareholders who exercise a power to convene a meeting under these provisions act as "quasi officials" of the company and must exercise the power to do so in the best interests of the company as a whole.[12]

Third, shareholders holding 5% or more of the votes that may be cast at the meeting may also themselves call and arrange to hold a general meeting,

[8] D Friedlander, M Fischer and M Ting, "Economic Activism: Re-Thinking Directors' Duties and Governance Structures in the Activist Context", Supreme Court of New South Wales Annual Corporate Law Conference, July 2014.

[9] *Corporations Act* s 249D. This section was amended by the *Corporations Legislation Amendment (Deregulatory and other Measures) Act* 2015 (Cth) to remove the earlier provision for 100 members to require a company to hold a general meeting.

[10] S Bielefeld et al, "Directors' Duties to the Company and Minority Shareholder Environmental Activism" (2004) 23 *C&SLJ* 28; S Shearing, "Raising the Boardroom Temperature? Climate Change and Shareholder Activism in Australia" (2012) 29 *EPLJ* 479.

[11] *Corporations Act* s 249E.

[12] *Humes Ltd v Unity APA Ltd* [1987] VR 474; (1987) 11 ACLR 641 at 646.

rather than requiring the company to do so.[13] In *Bisan Ltd v Cellante* (2000) 43 ACSR 322; [2002] VSC 430, that power was exercised to call a meeting to consider a resolution to remove the company's existing directors, and the Court observed that (at [10]) that the entitlement to call such a meeting:

> "recognises the importance of the right of a relatively small minority to be heard, to ventilate their concerns and to play an active role in the company's affairs."

Fourth, shareholders holding 5% or more of the votes that may be cast on a resolution may also require a company to place that resolution on the agenda for a general meeting.[14] The resolution must then be considered at the next general meeting that occurs more than two months after that notice is given, and the company must give members notice of that resolution at the same time, or as soon as practicable afterwards, and in the same way as it gives notice of the meeting.[15] Representatives of trade unions have relied on this provision on several occasions[16] and the Australasian Centre for Corporate Responsibility also put forward shareholder resolutions in respect of AGL Energy, ANZ and Origin Energy, seeking to amend the constitutions to achieve specified objectives in the 2015 annual general meeting season.[17]

Directors need not call such a meeting or place a resolution on an agenda for a meeting, and shareholders cannot call such a meeting, unless the resolution sought to be put to the meeting is within members' power.[18] That limitation can generally be avoided by framing a resolution as an amendment of the company's constitution, which a general meeting would have power to make[19], although such an amendment would require the higher voting threshold attached to a special resolution. This limitation was reconfirmed in *Australasian Centre for Corporate Responsibility v Commonwealth Bank of Australia* (2015) 107 ACSR 489; [2015] FCA 785[20], aff'd [2016] FCAFC 80, where ACCR gave notice to the Bank of resolutions that it proposed to move at the Bank's annual general meeting requiring the preparation of a report concerning the amount of greenhouse gas emissions financed by the Bank

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[13] *Corporations Act* s 249F.
[14] *Corporations Act* s 249N.
[15] *Corporations Act* s 249O.
[16] M Rawling, "Australian Trade Unions as Shareholder Activists: The Rocky Path towards Corporate Democracy" (2006) 28 *Sydney Law Review* 227 at 228; K Anderson and I Ramsay, "From the Picket Line to the Boardroom: Union Shareholder Activism in Australia" (2006) 24 *C&SLJ* 279; Black, note 6 above.
[17] Global Proxy Solicitation, *Corporate Governance Trends*, February 2016 at 8–11.
[18] *Alexander Ward & Co v Samyang Co* (1975) 1 WLR 673; *NRMA v Parker* (1986) 6 NSWLR 517; 11 ACLR 1; *Queensland Press Ltd v Academy Investments (No 3) Pty Ltd* [1988] 2 Qd R 575; (1987) 11 ACLR 419; *NRMA v Snodgrass* (2001) 37 ACSR 382; [2001] NSWSC 76; *Mortimer v Proto Resources & Investments Ltd* (2015) 107 ACSR 13; [2015] FCA 654.
[19] For examples of valid requisitions to amend the constitution, see *NRMA Ltd v Snodgrass* (2001) 37 ACSR 382, aff'd (2001) 39 ACSR 260; *NRMA v Parkin* (2004) 49 ACSR 386; [2004] NSWSC 296, appeal dismissed (2004) 49 ACSR 485; [2004] NSWCA 153; and the third proposed resolution in *Australasian Centre for Corporate Responsibility v Commonwealth Bank of Australia* (2015) 107 ACSR 489; [2015] FCA 785, aff'd [2016] FCAFC 80.
[20] For commentary, see M Hey, "ACCR v CBA [2015] FCA 785: Non-Binding Shareholder Resolutions and Implications for Shareholder Activism" (2015) 40 *University of Western Australia Law Review* 399.

and associated resolutions, including, as a third alternative, a special resolution to amend the Bank's constitution to require that such a report be prepared and released with the Bank's annual report. The Bank included the resolution for amendment of its constitution in the notice of annual general meeting, but declined to include the other resolutions on the basis that they were matters for the board and management and not capable of being considered by shareholders in general meeting, and that approach was upheld both at first instance and on appeal.[21] This relatively strict approach to the differentiation between shareholders' powers and management powers, confirmed in *Australasian Centre for Corporate Responsibility v Commonwealth Bank of Australia* above, excludes at least one mechanism that is available to activist shareholders in the United States, namely the passage of a non-binding resolution to place pressure on the board, subject to the remote possibility that a constitutional amendment could be passed by special resolution.

Directors may also refuse to call a general meeting, or place a resolution on its agenda, if matters could not be lawfully effected by the company in general meeting.[22] The decision in *Re Molopo Energy Ltd* (2014) 104 ACSR 46; [2014] NSWSC 1864 is a recent example of that principle. An activist shareholder there sought to require its directors to convene a general meeting to consider a resolution amending the company's constitution to authorise shareholders to reduce the company's capital. White J held that the proposed resolution was not within members' powers, on the basis that a reduction of the company's share capital could only be initiated by directors, where allowing shareholders an unqualified power to initiate a reduction of capital would lessen the protection otherwise available to creditors.[23] Directors may also refuse to call a general meeting if the requisition is for an extraneous purpose and constitutes an abuse of power.[24]

Fifth, shareholders with at least 5% of the votes that may be cast on a resolution may require the company to give a statement prepared by them relating to a proposed resolution or another matter that may properly be considered at a general meeting to other shareholders.[25] Shareholders generally may also ask questions about or make comments on the management of a company at a general meeting.[26]

Sixth, activist shareholders can also rely, by a somewhat indirect route, on the two-strikes rule in respect of remuneration to attack a company's wider policies, with 25% of votes cast against the remuneration report in successive

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[21] However, a general meeting may pass a resolution that has no immediate operative effect if that resolution would be a trigger for the exercise of a board discretion, for example, as to removal of the manager of a managed investment scheme: *Aveo Group Ltd v State Street Australia Ltd* [2015] FCA 1019 at [56], [65], aff'd [2016] FCAFC 81.
[22] *Windsor v The National Mutual Life Association of Australasia Ltd* (1992) 7 ACSR 210; 10 ACLC 509; *Re Molopo Energy Ltd* (2014) 104 ACSR 46; [2014] NSWSC 1864.
[23] For commentary, see E Boros, "Shareholders' Remedies: Altering the Division of Power between the Board and the General Meeting" (2015) 33 *C&SLJ* 129.
[24] *Australian Innovation Ltd v Petrovsky* (1996) 21 ACSR 218.
[25] *Corporations Act* s 249P.
[26] *Corporations Act* s 250S.

years triggering a requirement for a board spill resolution. A vote to spill the board is required if 25% or more of the votes cast at an annual general meeting are against adopting the company's remuneration report for two successive years.[27]

Seventh, an activist shareholder could bring an application to inspect a company's books under s 247A of the *Corporations Act* or for leave to bring derivative proceedings on behalf of a company under s 237 of the *Corporations Act*, but these are more costly and perhaps less predictable where they involve court applications. The scope for shareholder activists to rely on oppression proceedings in Australia is more limited, because Australian courts have tended to decline relief in oppression claims to shareholders who have "bought in" to the oppression, as a hedge fund activist would typically seek to do.

The role of institutional investors

There are open issues as to the role of institutional investors in supporting shareholder activism and the constraints on directors' powers. The role of institutional shareholders has received significant international attention, and several of the issues are noted in chapters in Professor Hill's and Professor Thomas' *Research Handbook on Shareholder Power*, the subject of the latter part of today's session.

In a chapter titled "Agency capitalism: further implications of equity intermediation"[28], Professor Gilson and Professor Gordon identify a shift from a position of widely dispersed shareholdings in the early 20th century, considered in Berle & Means' work[29], to large and concentrated institutional shareholdings which they describe as "agency capitalism". They note that intermediaries, particularly mutual funds in the United States, exhibit what they describe as "reticence" rather than "apathy" and point to various factors which tend against intermediaries initiating corporate actions. They recognise, however, an important implication of their analysis, namely that institutional investors may respond when an activist investor advances a strategic initiative, and that proposition is consistent with the recent rise of shareholder activism in the United States, with activist initiatives receiving significant support from institutional shareholders.

In a chapter surveying the evolution of institutional investors' role in corporate governance over thirty years, Professor Coates identifies increased influence of institutional shareholders, driven by improvements in the "technology of activism", the role of "investor agents", and diversity of institutional practice. Professor Bainbridge also addresses the relationship between "director primacy" and "shareholder interventions" and points to a range of matters that

[27] *Corporations Act* ss 250U–250V.
[28] This chapter follows on from an earlier article, R J Gilson and J N Gordon, "The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights" (2013) 113 *Columbia LR* 863.
[29] A Berle & G Means, *The Modern Corporation and Private Property*, 1932; see also WW Bratton & ML Wachter, "Shareholder Primacy's Corporatist Origins; Adolf Berle and *The Modern Corporation* (2008) 34 *J Corp L* 99.

limit shareholder activism by institutions, including that any gains from such activity are a "public good" which does not accrue only to the institution which has incurred the relevant cost, addressing similar issues to those identified by Professor Gilson and Professor Gordon. In a chapter dealing with the position in the United Kingdom, Professor Davies notes attempts by the United Kingdom government to promote greater activity by institutional shareholders, culminating in the introduction of a "quasi-official" Stewardship Code in 2010. Professor Davies also recognises, despite the efforts of government, that there remains substantial disincentives to institutional intervention, including the costs of intervention, the problem of free riding, such that any particular institution is likely to benefit from sharing in the gains of activism without incurring its costs; and conflicts of interest.

These issues are plainly significant for Australia, given the substantial size of retirement savings held in superannuation funds, and the fact that those funds are typically held in retail, industry or public funds managed by intermediaries which may have different objectives and incentives and will need to determine how to respond to activist initiatives.[30] Other significant institutional investors are, of course, life insurers, unit trusts and other managed funds. Traditionally, any activism of Australian institutional investors, like international institutional investors, has tended to be "defensive" in nature, undertaken where it has an existing stake in a company and identifies a decline in its performance for issues as to its corporate governance.[31] The cost, competition and "free riding" issues identified by the contributors to the *Research Handbook on Shareholder Power* are likely to reinforce that result.

However, that leaves an open question – will Australian institutions and proxy advisers in the Australian market, be as willing as US institutions, which share similar incentives and constraints, to support initiatives proposed by activist shareholders? The answer to that question may well be affected by the approach taken by proxy advisers, which may well influence institutional investors. For completeness, I should also recognise that there are other constraints on collective action by shareholders, if they give rise to an association for the acquisition of a relevant interest for the purposes of the takeover and substantial holding provisions in Chapter 6 of the *Corporations Act*, which are addressed by the Australian Securities and Investments Commission in its Regulatory Guide 128, *Collective Action by Investors*.

Constraints on directors

Some commentators have emphasised the constraints on directors' expenditure of corporate funds to defend against a campaign initiated by an activist shareholder.[32] In *Advance Bank Australia Ltd v FAI Insurances Ltd*

[30] For commentary, see G Stapledon, *Institutional Shareholders and Corporate Governance,* 1996; P Ali et al, *Corporate Governance and Investment Fiduciaries,* note 6 above; J Farrar and P Hanrahan, *Corporate Governance*, forthcoming.
[31] M Kahan and E Rock "Hedge Funds in Corporate Governance of Corporate Control" (2007) 155 *U Pa L Rev* 1021 at 1042; Cheffins and Armour, note 1 above at 56.
[32] D Friedlander et al, note 8 above. For a view that directors' powers are less constrained than Friedlander et al contend, see R Levy, "Aspects of the law relating to contested elections of directors" (2013) 33 *C&SLJ* 404.

(1987) 12 ACLR 118, Kirby P observed (at 137) that a board must not exercise its or a company's powers to promote only "a question of personality and not relevant to corporate policy" and Mahoney J observed (at [146]) that directors must "act in respect of the election for the good of the [company] as a whole"." Those propositions were applied by Barrett J in *Howie v Royal New South Wales Canine Council Ltd* [2006] NSWSC 565, albeit in a somewhat different context.

Directors must also be conscious of the need to provide a balanced disclosure to shareholders. In *Fraser v NRMA Holdings Ltd* (1995) 55 FCR 452 at 466, the Full Court of the Federal Court (Black CJ, von Dousa and Cooper JJ) observed that directors':

> "… fiduciary duty is a duty to provide such material information as will fully and fairly inform members of what is to be considered at the meeting and for which their proxy may be sought. The information is to be such as will enable members to judge for themselves whether to attend the meeting and vote for or against the proposal or whether to leave the matter to be determined by the majority attending and voting at the meeting."

In *Westchester Financial Services Pty Ltd v Acclaim Exploration NL* (1999) 32 ACSR 499; [1999] WASC 87 at [18], Owen J summarised the relevant principles as follows:

> "Directors are under a duty to make full disclosure of facts within their knowledge which are material to enable the members to determine upon their actions, including whether or not to attend the meeting and whether to seek further or additional information, either before or at the meeting. Directors seeking the passage of a resolution at a meeting of shareholders should provide shareholders with sufficient information concerning the business to be brought forward at the meeting. The shareholders must be put in a position to understand and form a judgment upon such business. Where directors take it upon themselves to urge or recommend that members exercise their powers in general meeting in a particular way ... it is an incident of the fiduciary obligation of directors that adequate information be provided."

This issue also arose in *ENT Pty Ltd v Sunraysia Television Ltd* (2007) 61 ACSR 626; 25 ACLC 399; [2007] NSWSC 270, where a shareholder sought to injunct a shareholders' meeting on the ground that directors had failed to provide such information as would fully and fairly inform shareholders of the matters to be considered at the meeting. Austin J observed (at [20]) that the adequacy of information provided in an explanatory memorandum for a shareholders' meeting is to be assessed in a practical, realistic way having regard to the complexity of the proposal; and to be judged by reference to the effect of the document on an ordinary person who read it quickly, and whether any deficiency in it would cause shareholders to vote, or abstain from voting, under a serious misapprehension. His Honour also observed (at [21], [25]) that shareholders are entitled to receive information that is material to the question whether a transaction proposed by directors should be approved, including material commercial information which is known to or accessible to directors. His Honour noted (at 48]) that, where shareholders' approval was sought for a proposal by a company to sell its main undertaking, the directors' duty to properly inform shareholders required them to disclose their opinion as to whether the sale price was a fair price and the basis for that opinion.[33]

An activist shareholder would arguably not be subject to a similar constraint. There is an open question whether information provided in respect of shareholders meetings is within the scope of s 1041H of the *Corporations Act*, where it may not have the requisite connection with financial products, and whether it is provided in trade or commerce for the purposes of the prohibition on misleading or deceptive conduct in s 18 of the *Australian Consumer Law* or the corresponding provisions in the state *Fair Trading Acts.*[34] An attack based on misleading or deceptive conduct may also have limited prospects where issues involve matters of advocacy and opinion. The business judgment rule will provide limited protection to directors in a contest with an activist shareholder, since it is limited to the duty of care and diligence and does not extend to the proper purposes obligation.[35]

Book Launch of Research Handbook on Shareholder Power

I am also delighted to have the opportunity to launch the weighty text edited by Professor Jennifer Hill and Professor Randall Thomas titled *Research Handbook on Shareholder Power*. Professor Hill is, of course, well known to all of us, as Professor of Corporate Law at the Law School of the University of Sydney. Professor Thomas is John S. Beasley II Professor of Law and Business at Vanderbilt University Law School, and also no stranger to Australia. This book weighs in at a solid 610 pages, excluding the index, and comprises a useful introduction by Professors Hill and Thomas and 27 chapters divided into categories.

Professor Hill's and Professor Thomas' introduction provides something of a summary of the range of articles found in the work. That introduction starts with the illuminating observation that much of the history of corporate law is concerned, not with shareholder power, but with its absence. It is a sign of radical change that a significant amount of professional and academic attention in the United States is now directed to the risk that smaller groups of shareholders, particularly hedge funds, can capture the agenda of public companies.[36] This is the antithesis of the long recognised risk that management may operate companies with little control by a diverse and seemingly powerless, or at least inert, body of shareholders.

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[33] For commentary, see R Teele Langford, "ENT Pty Ltd v Sunraysia Television Ltd: A Positive Fiduciary Duty of Disclosure" (2008) 26 *C&SLJ* 570.

[34] *Yates v Whitlam* (1999) 32 ACSR 595 at [14]–[16]; *Cleary v Australian Co-Operative Foods Ltd (No 3)* (1999) 32 ACSR 701; *NRMA Ltd v Yates* (2000) 18 ACLC 45 at 50–53.

[35] D Friedlander et al, note 8 above.

[36] For a small sample of the voluminous literature, see Cheffins & Armour, "The Past, Present, and Future of Shareholder Activism by Hedge Funds", note 1 above; L Bebchuk, "The Myth that Insulating Boards Serves Long-Term Value" (2013) 111 *Colum L Rev* 1637; BS Sharfman, "Activist Hedge Funds in a World of Board Independence: Creators or Destroyers of Long-Term Value" (2015) *Colum Bus L Rev* 813; Bebchuk et al, "The Long-Term Effects of Hedge Fund Activism" note 3 above; D Katelouzou, "Worldwide Hedge Fund Activism: Dimensions and Legal Determinants" (2015) 17 *U Pa J Bus L* 789; JC Coffee Jr & D Palia, "The Wolf at the Door: The Impact of Hedge Fund Activism on Corporate Governance" (2016) 41 *J Corp L* 545.

Professor Hill and Professor Thomas identify a major shift in capital market structures which, they rightly recognise, requires a reassessment of the role and power of shareholders, although they also recognise, again rightly, that there is an open question as to the extent to which that shift has been reflected in Australia. Professor Hill's and Professor Thomas' introduction also identifies several major themes in the work, including:

- differences in the distribution of shareholders, between a position of dispersed ownership as is common in the UK and the US and block ownership which may be the international norm;
- a dichotomy between shareholder protection on the one hand and shareholder participation or shareholder power on the other;
- the status of the "law matters" hypothesis, advanced by La Porta and others[37], which postulated a connection between the structure of corporate law, including shareholder protection, and the economic performance of capital markets;
- the question whether stronger shareholder powers are desirable as a matter of policy;
- the distinction between "law on the books" and law in action; and
- questions as to the effectiveness of transplanting legal structures from one jurisdiction to another.

In the short time I have today, I cannot provide anything approaching a detailed review of these 27 chapters, and it is not necessary for me to do so where Professor Hill and Professor Thomas provide a sampling in their introduction to the text. I do, however, want to point to some highlights, at least from my perspective.

Part I deals with the history of shareholder power, and contains two broader discussions of shareholder power. I have referred above to Professor Gilson's and Gordon's interesting chapter noting the reluctance of intermediaries to initiate, as distinct from supporting, activist initiatives. Professor Hill's chapter "Images of the shareholder – shareholder power and shareholder powerlessness" points to alternative characterisations of shareholders as excluded from power, as gatekeepers, or, since the global financial crisis, as victims or collaborators in corporate mismanagement. She recognises the dominance of institutional investors in the United States, United Kingdom and Australia but makes the important observation that that position is not necessarily reflected elsewhere. She also notes the significant difference between Australia, where public enforcement by the Australian Securities and Investments Commission plays an important role in the enforcement of director's duties, and the position in the United States and the

[37] See, for example, R La Porta et al., 'Corporate Ownership Around the World' (1999) 54 *Journal of Finance* 471; R La Porta et al, "The Economic Consequences of Legal Origins", (2008) 46 *J of Economic Literature* 285.

United Kingdom where such enforcement is largely left to private litigation. She also recognises that the structure of US law, and particularly Delaware law, creates a limited risk of liability for breach of director's duties, by contrast with the real risk of such liability under Australian law.

Part II deals with categories of shareholders, including institutional investors, hedge funds, controlling shareholders and contains an additional chapter dealing with the State as a shareholder in China. I have referred to Professor Coates' chapter in this part above. This Part also contains two chapters dealing with activist hedge funds in the United States and Europe. Professor Partnoy deals with the rise of activism by hedge funds in the United States. He recognises the controversy as to whether hedge funds are the solution to the separation of ownership and control which so troubled Berle & Means or are alternatively "financial villains"; he offers a definition of hedge funds and points to increased focus on their regulation following the Dodd-Frank Wall Street Reform and Consumer Protection Act 2010 (US); and also deals with the issues raised by the separation of voting and economic interests by derivative products. This issue has, of course, long been recognised in Australia in the takeover context. A further chapter notes that hedge fund activism in Europe is less visible than such activism in the United States and that interventions may occur less publicly in Europe than in the United States. Other chapters identify issues arising from controlling shareholdings in family business groups in other jurisdictions and a chapter deals with the particular issues arising from the State as a controlling shareholder in China.

Part III deals with the relationship between shareholders and the board of directors. I have referred to Professor Bainbridge's comments as to intervention by institutions above. Professor Bainbridge also addresses the particular forms of intervention by hedge funds, including attempts to target perceived undervaluation of companies, promote change in corporate governance, promote changes in a target's capital structure, promote changes of control or bring about changes in a target's business strategy. He points to evidence of gains to shareholders from such activities, particularly in respect of control transactions, but argues for a need for scepticism as to hedge fund interventions seeking to change business strategy.

Professor Blair's chapter in Part III considers the role of directors, viewed from the perspective of the "team production model" which Professors Blair and Stout have long advocated. A further chapter considers the role of independent directors and controlling shareholders in jurisdictions where that question is less commonly studied, including continental Europe, Japan, Brazil, Russia, India and China, and addresses some of the challenges to the application of that model in those jurisdictions. Part IV is titled "Shareholder Power in Action" and deals with several current issues including takeovers, equity based compensation, "say on pay" and issues of jurisdiction in shareholder litigation.

Part V provides several international perspectives on shareholder power, including a useful and lengthy chapter by Professor Davies of the University of Oxford dealing with the United Kingdom. Professor Davies points to the extent of dispersed shareholdings in the United Kingdom and to the decline of domestic ownership of UK shares, and a potential reduction in shareholder activism in consequence. There is, of course, an interesting question as to the extent to which this may change in a post-Brexit United Kingdom. I have noted Professor Davies' comments as to the role of institutional investors above. Professor Davies also distinguishes activism that is defensive in character, responding to adverse developments in a company where an institution holds an investment, and "offensive" activism, primarily associated with hedge funds, which involves the acquisition of a non-controlling stake in order to influence the company's activities and profit from the result. Professor Davies also points to the extent to which institutional shareholders have been successful, in a largely self-regulatory context, in promoting "shareholder-friendly" rules, including the "one vote one share" principle and a significant role for non-executive directors.

This Part also includes two other chapters dealing with the position in Italy and Germany which show very different shareholding patterns and governance structures to the US, UK and Australia. This Part also includes two chapters dealing with the position in the United States, including reference to shareholder power in the United States and corporate voting in US public companies and a chapter dealing with changes in ownership structures and shareholder power in Brazil.[38] There are five chapters dealing with the position in Asia. However, despite Professor Hill's role as joint editor, this Part delivers a humbling lesson in economic reality and does not extend to the position in Australia.

This is a very worthwhile book, not only for an international audience but also for this distant corner of the world. Australian readers with an interest in corporate law will find matters of interest in many chapters. The book is a thought-provoking and welcome resource for thinking about questions of corporate governance and the questions addressed today as to whether we will see greater levels of shareholder activism driven by economic objectives.

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[38] See also PH Edelman, RS Thomas and RB Thompson, "Shareholder Voting in an Age of Intermediary Capitalism" (2014) 87 *S Cal L Rev* 1359.