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Proxy Contests for Corporate Control

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Proxy Contests for Corporate Control. (2d ed.). EDWARD ROSS ARANOW and HERBERT A. EINHORN. New York: Columbia University Press. 1968. Pp. xviii, 692. $35.00.

"America's publicly owned companies control the disposition of the great bulk of our nation's productive facilities. The manner in which the directors of those companies are selected, and the manner in which that selection is legitimized, are therefore matters of intense concern to all of us."[1]

There is, of course, no secret about how the directors of America's publicly-owned companies are selected. Generally, they are selected by the managers and the other directors, although there are instances where particular directors are chosen to represent the interests of substantial shareholders,[2] creditors, customers or other parties interested in the conduct of the company's affairs. In most cases, selection is legitimized by submitting the names of the nominees to the shareholders for ratification. The nominees, or some of them, appear at a quaint ritual, called the "annual meeting," to submit to questions, and perhaps some taunts, from assembled shareholders.

The focus of this book, however, is on the situation that arises when another self-chosen group of men decide that they would like to take over the management of a particular company. The result is a contest to see which side can obtain proxies from the holders of a majority of the shares. Shares are held by individuals, of various ages and persuasions, by banks and brokers for the accounts of individuals, by other corporations, and, to a rapidly increasing extent, by so-called "institutional investors"—pension funds, investment companies, insurance companies, charitable and educational institutions, and other types of arrangements under which the people who vote the shares have no other beneficial interest in them. To ascertain what influence, if any, these different classes of investors have or could have on corporate policies and selection of management, one would like to know what attitudes they take in proxy contests and to what types of appeals they respond in choosing between opposing groups of candidates. Unfortunately, that is not what this book is all about. Beyond the brief suggestion that the most effective issues for insurgents are those

1 P. xiii (opening sentences of Introduction by Manuel F. Cohen, former Chairman of the Securities and Exchange Commission).

2 In Feder v. Marietta Corp., 406 F.2d 260 (2d Cir. 1969), one corporation was held liable for short-swing profits as a "director" of another corporation under Section 16(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78p (1964), on the ground that it had "deputized" its president to represent its interests on the board of the other corporation.

based on poor earnings and dividends or attacks on the integrity of management,[3] and that management can best respond by undertaking "a dramatic new program which will have stockholder appeal,"[4] there is no analysis of the substance of these political struggles for control of the governmental apparatus of the corporations.[5]

This is a book for people who are involved in proxy contests rather than for people who want to study them.[6] As might be expected, the temptations presented by the perquisites of corporate management have led both insurgents and incumbent managements to employ "often reckless, uninformative, or misleading charges and counter-charges,"[7] to the point that the Securities and Exchange Commission in 1956 adopted special rules applicable to election contests to supplement the rules applicable to proxy solicitations generally.[8] It is with the operation of these rules, as well as with the state laws governing the conduct of election meetings, inspection of stockholder lists and similar matters, that Aranow and Einhorn are principally concerned. They also cover the availability of judicial remedies, the expenses of proxy contests, and the resources available for various types of proxy solicitation. Their book is a thoroughly professional, well-organized and well-written guide to the legal and procedural aspects of proxy contests.

Both the preface and the introduction claim increased significance for the proxy rules as a result of developments since the first edition of the book appeared in 1957. The most notable developments were the 1964 amendments extending federal proxy regulation to more than three thousand large companies whose securities are traded over the counter,[9] and the Supreme Court's holding in *J. I. Case Co. v. Borak*[10] that a shareholder could enjoin corporate action based on proxies solicited in violation of SEC rules. But, as a result of more recent developments which the authors also note, the proxy contest in its pure form has in the past couple of years become a distinctly secondary, and is perhaps on its way to becoming a largely obsolete,

3 P. 11.

4 P. 24.

5 The book might be compared to a study of the American electoral process which focused primarily on the procedures and decisions of the Fair Campaign Practices Committee.

6 That is presumably what justifies a price of $35.00 for a book with approximately 600 pages of text.

7 P. xiv.

8 17 C.F.R. § 240.14a-11 (1968).

9 Securities Acts Amendments of 1964, 15 U.S.C. § 78*l*(g) (1964).

10 377 U.S. 426 (1964).

road to control of a publicly-held company. Outsiders have discovered that it may be a lot easier, and indeed cheaper, to buy up a majority of the shares of the target company than to solicit the votes of its present shareholders. Also, while the loser in a proxy contest has nothing to show for his time and expense but some worthless pieces of paper, the loser in a purchase contest is often able to sell out his interest to the winner for a tidy profit.[11] As against twenty-seven proxy contests filed with the SEC during the year ended July 31, 1968,[12] there were an estimated two hundred forty-nine tender offers during 1968 seeking a controlling or substantial interest in a publicly-held company.[13] Many of these tender offers, needless to say, have evidenced the same kinds of "reckless, uninformative, or misleading charges and countercharges" that had characterized proxy contests. The congressional response was the enactment in July 1968 of amendments to the Securities Exchange Act of 1934 imposing disclosure requirements, comparable to those found in the proxy rules, on anyone who solicits shareholders to accept or reject a tender offer.[14] Aranow and Einhorn have a brief closing chapter on tender offers, and much of their discussion of the standards applied by the SEC staff to disclosures in proxy statements will also be applicable when disclosures in connection with tender offers are being reviewed by the same staff.

Of course, the rise of the tender offer has thoroughly exposed (if indeed any further exposure was needed) the ineffectiveness of the present shareholder voting requirement, based as it is on the rule of "one share, one vote," in placing any "democratic" limitations on the selection or activities of corporate managers. A system in which a man or company can win an election by buying up a majority of the votes can hardly be called democracy, no matter how broadly that term is defined. In the past, there has been at least a plausible argument that the large shareholder was entitled to more votes because of his larger stake in the company's operations, but now that accomplished take-over artists have learned how to buy up a company's shares by using the company's own assets,[15] the substance of that argument has been hollowed out even further.[16]

11 *See* Burck, *The Merger Movement Rides High*, FORTUNE, Feb. 1969, at 79, 158, 161.

12 1968 SEC ANN. REP. 42.

13 Burck, *supra* note 11, at 80.

14 15 U.S.C.A. § 78n(d) (Supp. 1969), *amending* 15 U.S.C. § 78n (1964).

15 *See* Burck, *supra* note 11, at 158.

16 The "corporate democracy" myth still has a firm hold, however. The New York Stock Exchange recently expressed concern over the tactics adopted by incumbent managements to thwart prospective take-overs by establishing insurmountable voting

There have been some suggestions of movement, but so far very few concrete steps, toward the objective of making corporate managers more responsible to their various classes of constituents through truly democratic procedures. Those steps may yet be some distance off, and if you are involved in the proxy contest game, Aranow and Einhorn give you the rules that govern it at the present time.

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requirements for mergers and similar transactions, on the ground that these measures would tend to discriminate against certain shareholders. *See* Wall St. J., Feb. 20, 1969, at 6, col. 2; *id.* Feb. 21, 1969, at 7, col. 1.

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