THE SHAREHOLDER RIGHTS AND ACTIVISM REVIEW

FOURTH EDITION

Editor
Francis J Aquila

THE LAWREVIEWS

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PREFACE

In the years since the last financial crisis, shareholder activism has been on the rise around the world. Institutional shareholders are taking a broad range of actions to leverage their ownership position to influence public company behaviour. Activist investors often advocate for changes to the company, such as its corporate governance practices, financial decisions and strategic direction. Shareholder activism comes in many forms, from privately engaging in a dialogue with a company on certain issues, to waging a contest to replace members of a company's board of directors, to publicly agitating for a company to undergo a fundamental transaction.

Although the types of activists and forms of activism may vary, there is no question that shareholder activism is a prominent, and likely permanent, feature of the corporate landscape. Boards of directors, management and the markets are now more attuned to and prepared for shareholder activism, and engaging with investors is a priority for boards and management as a hallmark of basic good governance.

Shareholder activism is a global phenomenon that is effecting change to the corporate landscape and grabbing headlines not only in North America but also in Europe, Australia and Asia. Although shareholder activism is still most prevalent in North America, and particularly in the United States, almost half of the publicly announced activism campaigns in 2018 targeted non-US companies. This movement is being driven by, among other things, a search by hedge funds for new investment opportunities and a cultural shift toward increased shareholder engagement in Europe, Australia and Asia.

As both shareholder activists and the companies they target have become more geographically diverse, it is increasingly important for legal and corporate practitioners to understand the legal framework and emerging trends of shareholder activism in the various international jurisdictions facing activism. *The Shareholder Rights and Activism Review* is designed as a primer on these aspects of shareholder activism in such jurisdictions.

My sincere thanks to all of the authors who contributed their expertise, time and labour to this fourth edition of *The Shareholder Rights and Activism Review*. As shareholder activism continues to diversify and increase its global footprint, this review will continue to serve as an invaluable resource for legal and corporate practitioners worldwide.

Francis J Aquila
Sullivan & Cromwell LLP
New York
August 2019

Chapter 1

AUSTRALIA

Quentin Digby and Timothy Stutt[1]

I OVERVIEW

The past 18 months have seen an intense, and growing, focus on corporate culture and accountability in Australia, which has in turn driven increasing activism at listed Australian companies, particularly in the financial services sector. As opposed to hedge fund activism focused on extracting economic gains, or retail shareholder activism focused on environmental, social and governance (ESG) issues, a lot of the recent developments in shareholder activism in Australia have been driven by large, erstwhile 'passive', institutional investors manifesting their displeasure at a perceived lack of accountability within their portfolio companies.

In large part, this focus on corporate culture and accountability has been driven by systemic failings in risk management and compliance, which were highlighted by the recent Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (the Financial Services Royal Commission). The Financial Services Royal Commission, which was conducted through public hearings, generated significant media attention and captured the attention of the Australian investment community and the community at large. Particular criticism related to how Australian financial services companies manage non-financial risk and the lack of responsiveness of some companies' remuneration systems to poor risk outcomes or corporate culture.

While Australia's banks remain very profitable and among the most prudentially sound financial institutions globally, external stakeholders ranging from regulators and the government through to institutional investors expressed concern at the apparent failings in oversight and the lack of attention to retail customer interests. This has been a significant contributing factor to three of the four major Australian banks receiving large protest votes against the adoption of their remuneration reports and has coloured much of the continuing public dialogue around governance, corporate accountability and stakeholder expectations over the past year.

II LEGAL AND REGULATORY FRAMEWORK

The Australian regulatory framework is conducive to activist campaigns with clear statutory rights afforded to shareholders in respect of accessing the company's register of shareholders and contacting its shareholders, nominating and removing directors, and requisitioning

1 Quentin Digby is a partner and Timothy Stutt is a senior associate at Herbert Smith Freehills. The authors would also like to acknowledge the assistance of Barry Wang, solicitor, and Emily Mackay, paralegal, at Herbert Smith Freehills.

resolutions and calling shareholders' meetings. Further, Australian listed companies are not permitted to have 'poison pills' and almost universally have a single class of ordinary voting shares, as required by the Australian Securities Exchange (ASX). However, in spite of this, there are certain defences and structural advantages available to boards and management of listed companies in Australia when responding to activist campaigns.

i Contacting shareholders

Under the Corporations Act 2001 (Cth) (the Corporations Act), companies are required to allow anyone to inspect their register of shareholders. The Corporations Act also provides a process for people to request copies of the register of shareholders. This statutory right is commonly used by shareholder activists to gather shareholders' contact details to write to them regarding activist proposals or to solicit votes in respect of upcoming shareholders' meetings.

By accessing the register (or obtaining a copy of the register), a person would obtain each shareholder's name and address, as well as details regarding his or her holding in the company (Section 169 of the Corporations Act). At present, the information does not include email addresses as these are not prescribed details for inclusion in the register under Section 169. A law reform proposal was introduced in 2017 to include email addresses on company registers. However, the Australian Senate rejected the draft legislation in its proposed form and the proposal has stalled for the time being (see Section V).

It is an offence to use information about a person listed in the register to contact or send material to him or her, unless the use or disclosure of that information is relevant to the shareholding of that person or to the rights attaching to the shareholding (Sections 177(1) and (1A) of the Corporations Act). However, in most cases, activist proposals will comply with this requirement as they would typically be relevant to the exercise of votes by shareholders. Where shareholder activists send material to shareholders that is inaccurate or that the company's board considers is misleading, there are a number of avenues open to the board, including taking action against the activists for engaging in misleading or deceptive conduct or, potentially, defamation.

The register of shareholders only contains the names and details of the legal holders of shares (i.e., not the underlying beneficial holders). This can create a significant barrier to shareholder activists contacting shareholders, as it means that they are reliant on the timely relay of information by intermediaries and custodians. A separate register of relevant interests held in the company's shares, including beneficial interests, is also required to be kept by the company under the Corporations Act. However, these registers only contain information regarding shareholders' beneficial interests where it has been specifically requested by the company pursuant to a 'tracing' notice and the data is often not helpful to shareholder activists or other users (as companies are only required to share the raw data and not their internal analysis of underlying beneficial interests, which provides a greater insight into the company's ownership).

Of course, as a substitute for corresponding with each shareholder, activists typically limit their direct engagement to the key underlying institutional shareholders and then rely on print and social media for indirect engagement with the balance of the register, including retail shareholders (as well as to exert pressure on the board).

ii Calling shareholders' meetings

It is relatively straightforward for shareholder activists to call or requisition a meeting of shareholders under the Corporations Act to formally consider and vote on activist proposals. The Corporations Act also includes a process for shareholders to requisition additional resolutions for consideration at an upcoming scheduled shareholders' meeting.

Shareholders holding 5 per cent of the votes in a company can requisition a shareholders' meeting under Section 249D of the Corporations Act. Where a meeting is duly requisitioned according to this process, the company's directors are required to convene the meeting within two months of the requisition and the company must meet the relevant costs of holding it. A shareholder request for these purposes must be in writing, state any resolution to be proposed at the meeting, be signed by the members making the request and be properly given to the company. Failure to follow these procedural requirements can invalidate the requisition and companies can, and commonly do, refuse to convene meetings where they are not complied with. The directors may also refuse to convene the requisitioned meeting where the subject of the meeting is a matter that is not validly within the power of shareholders.

Where a meeting is requisitioned using the process in Section 249D, decisions regarding the content of the notice of meeting will be determined by the board of the company (as in the normal course). However, shareholders holding 5 per cent of the votes or at least 100 shareholders are entitled to request that a statement be included with the notice of meeting setting out their views (Section 249P), and there are limited grounds on which companies may refuse to comply with this requirement. Companies may refuse the request where the statement is more than 1,000 words long or defamatory. Although the shareholders would be requisitioning the meeting, almost without exception the company's chair would have the right to chair the meeting under the company's constitution. Accordingly, companies are able to control the conduct of proceedings of the meeting, including any debate on an item of business, subject to the usual rules regarding the conduct of meetings and duties of the chair.

The Corporations Act also includes an alternative process for shareholders to convene a meeting, in which case they would be in a position to determine the time and venue of the meeting and the content of the initial notice of meeting, but also be liable to pay the expenses of calling and holding the meeting themselves (e.g., printing, postage and venue costs). Under Section 249F, shareholders with at least 5 per cent of the votes that may be cast at a general meeting of the company may call, and arrange to hold, a meeting. Calling a shareholders' meeting according to this process provides activists with a strategic advantage in that they can control the timing and location of the meeting (subject to the overriding requirement that it be held at a reasonable time and place), as well as the content of meeting materials, including the notice of meeting. Again, the chair of the company is likely to be able to chair the meeting under the company's constitution and control the conduct of the meeting. Despite its advantages for shareholder activists, this alternative process is infrequently used in Australia given the considerable costs it can entail for the convening shareholder.

iii Requisitioning additional resolutions for scheduled shareholders' meetings

Where there is already a shareholders' meeting in contemplation (e.g., the company's annual general meeting (AGM)), an alternative process, commonly used by retail shareholder activists, is to requisition additional resolutions for consideration at that upcoming meeting. Under Section 249N of the Corporations Act, 100 shareholders or shareholders with 5 per cent of the company's votes may give a company notice of a resolution that they propose to move at a general meeting.

Similar to requisitioned meetings, the notice must be in writing, set out the wording of the proposed resolution and be signed by the members proposing to move the resolution. The company does not need to give notice of the resolution if it is more than 1,000 words long or defamatory. However, it is otherwise required to give notice to shareholders that the resolution will be considered at the next general meeting that occurs more than two months after the notice is given and, provided it is received in time, the company must meet the costs of giving shareholders notice of the requisitioned resolution.

Because this process allows for 100 shareholders (with shareholdings of any size) to requisition resolutions, it is the preferred mechanism for social and environmental shareholder activists to agitate for changes in company's operations and policies. With the power of social media increasing, what was once a significant logistical hurdle has become a far simpler requirement for social and environmental activists to meet. As a result, campaigns from groups such as the Wilderness Society and the Australasian Centre for Corporate Responsibility (ACCR) have become relatively common for ASX-listed companies.

As a matter of procedure (though it can also be relevant to strategy), where a requisition is received from a shareholder, irrespective of whether it is valid, the company is required to make an ASX release within two business days. This creates significant timing pressure for companies in developing their response strategy to a requisition.

Under Australian law, the board can dismiss a requisitioned resolution if it purports to direct the board how to exercise its powers of management (as set out in its constitution). Generally, to supplant the powers vested in the board, such 'directions' would be required to be enshrined in the constitution (with a special resolution requisitioned to amend the constitution for that purpose). This position has been confirmed by the Full Court of the Federal Court of Australia,[2] although there have also been calls from the Australian Council of Superannuation Investors (ACSI) for regulatory reform to enable requisitioned non-binding advisory resolutions to be permitted.[3]

iv Nominating and removing directors

Australian companies typically have very low thresholds in their constitutions for shareholders to nominate a person for election to the board of the company. Unlike other comparable jurisdictions, Australian law does not mandate a threshold level of shareholder support for an external candidate to be nominated to the board of a listed company. In most cases, a single shareholder (with a holding of any size) will be able to nominate a person for election to the board of a company and need only comply with the specific timing requirements in the relevant company's constitution.

Because of the simplicity of this nomination process (which requires no minimum baseline level of support), it has occasionally been used by shareholder activists in place of requisitioning resolutions as a platform to advance criticisms of the company or agitate for changes to the company's processes or operations. For the company, an external nomination can involve additional expense and distraction beyond what would otherwise be required with a requisitioned resolution or statement. In particular, additional care and attention is required, from a governance perspective, in dealing with any director nomination.

2 *Australasian Centre for Corporate Responsibility v. Commonwealth Bank of Australia* [2016] FCAFC 80.

3 See Australian Council of Superannuation Investors, *Shareholder Resolutions in Australia* (research report), 2017.

The external candidate will typically be elected if he or she secures a simple majority of votes cast at the shareholders' meeting, unless the company is at its constitutionally mandated maximum board size. Where the company is at its maximum number of directors, the candidate will need to outpoll one of the incumbent directors standing for re-election at the meeting.

The Corporations Act also sets out a specific process for shareholders that wish to remove a director from the board of a public company. This process applies regardless of anything in the company's constitution, though in some cases the constitution may provide additional avenues for removing directors.[4]

To validly requisition a resolution to remove one or more directors, the shareholder must give notice of its intention to move the resolutions and comply with the process for requisitioning a resolution (outlined in subsection iii). The notice of intention must be given to the company at least two months before the meeting is to be held (Section 203D(2) of the Corporations Act). The company must give the relevant director or directors a copy of the notice as soon as practicable after it is received and the director is entitled to put his or her case to shareholders by giving the company a written statement for circulation to members and speaking to the motion at the meeting.

v Other avenues available to activist shareholders

Public listed companies in Australia are required under the ASX Listing Rules to hold an election of directors each year at their AGM and this provides an opportunity for activist shareholders to lodge a protest vote against particular directors or block the re-election of incumbent directors to agitate for board succession.

Australian listed companies are also required to put an advisory resolution to their shareholders for adoption of the remuneration report at each AGM and, in recent years, this has been co-opted by some activist shareholders as a protest mechanism against the company's current management or operations (i.e., for issues outside of executive remuneration). Additionally, where a company receives an against vote of at least 25 per cent of the votes cast in two consecutive years (receiving 'two strikes'), a board spill resolution must be put to shareholders that, if passed, will require that the non-executive directors of the company stand for re-election at a special 'board spill meeting' of the company if they wish to continue in office. Although intended to address issues related to the remuneration practices of companies, this mechanism is open to abuse by shareholder activists as an indirect means of suggesting a spill of the board and placing pressure on the company's directors. The two strikes rule can also be practically difficult for directors from a duties perspective, given that it essentially relies on directors being influenced by factors extraneous to the core principle of what is in best interests of the company.

In extreme circumstances, shareholder activists may bring derivative proceedings against the company's directors under Section 236 of the Corporations Act (being a claim brought on behalf of the company) or seek court orders to address conduct that is oppressive to shareholders under Section 233 of the Corporations Act.[5] Although these types of proceedings rarely proceed to trial in Australia, hostile shareholder activists will occasionally put the

4 See, for example, the recent case of *State Street Australia Ltd in its capacity as Custodian for Retail Employees Superannuation Pty Ltd (Trustee) v. Retirement Villages Group Management Pty Ltd* [2016] FCA 675.

5 See, for example, the case of *RBC Investor Services Australia Nominees Pty Limited v. Brickworks Limited* [2017] FCA 756.

company on notice that they are contemplating such proceedings as a means of encouraging the swift resolution of issues under negotiation. In some cases, proceedings may be instituted; however, this is a high-stakes manoeuvre for activist shareholders as the courts have the power to award costs against the party bringing the action (including full costs indemnification, where appropriate). The Corporations Act includes a process for shareholders or persons bringing derivative actions to apply to the court for access to the company's documents. Although any such application must be made in good faith and for a proper purpose, it can be used by shareholder activists to help them build a case against the incumbent board or management, including as a way to build their case for instituting a derivative action.

vi Considerations for boards in responding to activist campaigns

In responding to any activist campaign, the board of the relevant company must have regard to their duty to act in the best interests of the company and for proper purposes. Relevantly, under the principles set out in the *Advance Bank* case,[6] limitations are placed on the board's use of company funds to 'campaign' in relation to contested director elections.

It is relatively unusual in Australia for high-profile companies to be subject to contested director elections involving shareholder mail-outs and extensive lobbying by activist investors. For that reason, the legal limits on how companies can respond to such campaigns are not well defined. However, case law in Australia (including the *Advance Bank* case) does allow for:

a directors to make recommendations to shareholders where they genuinely believe that it is desirable for shareholders to know their views on matters before the meeting; and

b the communication to shareholders of information that is material to their decision on how to vote on the external nomination or shareholder-requisitioned resolutions.

Directors have a duty to provide shareholders with any material information they have in relation to a shareholder activist proposal to ensure that voting proceeds on an informed basis. This permits the directors to rebut inaccurate aspects of activist proposals or present counterarguments for consideration by shareholders (i.e., informing shareholders). It will not, however, extend to the board telling shareholders how to vote on proposals (i.e., urging shareholders) or engaging in debates over issues of personality.

The board's toolkit for responding to a contested director election scenario or other activist proposal would typically include the following:

a formulation of a board recommendation in relation to the external nomination or shareholder requisition;

b high-level meetings between directors and substantial shareholders;

c the sending of specific hard copy or email communications to shareholders; and

d establishment of a shareholder hotline to receive inbound calls from shareholders to answer questions regarding the external nomination or shareholder-requisitioned resolutions.

In some cases, companies may also engage a proxy solicitation firm to make outbound calls to shareholders. This involves a higher level of risk from an *Advance Bank* perspective, unless it is strictly limited in scope to ensuring that shareholders are aware of the issue (and the relevance of their vote) and the costs involved are reasonable. However, depending on the intensity of

6 *Advance Bank Australia Ltd v. FAI Insurances Ltd* (1987) 9 NSWLR 464; 12 ACLR 118.

the activist campaign, the company may be justified in taking more assertive steps to ensure that shareholders are receiving balanced and accurate information, including the use of proxy solicitation firms.

III KEY TRENDS IN SHAREHOLDER ACTIVISM

i Increased focus on ESG matters

Climate change has long been a focus during questions at AGMs for listed companies in the insurance, energy and resources sectors in Australia. However, in the past few years, Australia has increasingly seen requisitioned resolutions concerning ESG matters brought by environmental or social activist groups at companies' AGMs and this trend has continued during the most recent AGM season.

Ahead of the AGMs for oil and gas producers, Santos and Woodside, resolutions were attempted to be requisitioned to amend the companies' constitutions and to request additional disclosure concerning alignment of the businesses with the Paris Climate Agreement and emissions targets (as well as a review of the companies' positions, oversight and processes relating to public policy advocacy). Both the resolutions were able to be rejected as the activist group had not complied with the Corporations Act's procedures for requisitioned resolutions (see Section II.iii).

Other examples of prominent Australian listed companies that received requisitioned resolutions in the past 12 months include:

a energy provider and retailer Origin: Origin received requisitioned resolutions to amend its constitution, to expand its measurement and reporting of methane emissions and to disclose details about the process for seeking consent of the traditional owners of the land for a proposed project;

b coal-miner Whitehaven: Whitehaven received requisitioned resolutions to amend its constitution and to implement disclosure about climate-related risks in accordance with the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures;

c international air carrier Qantas: Qantas received requisitioned resolutions to amend its constitution and to implement heightened human rights due diligence and policies regarding deportation of refugees and asylum seekers on the airline's services; and

d national supermarket retailer Woolworths: Woolworths received requisitioned resolutions to amend its constitution and requesting it to reach an agreement with the National Union of Workers to introduce a pre-qualification programme ostensibly directed at labour hire providers' compliance with labour and human rights standards in Woolworths' supply chain.

In all cases, the requisitioned resolutions failed to be passed by shareholders at the relevant companies' AGMs.

ii Increased prominence of overseas 'economic' activists in the Australian market

Traditionally, the Australian experience with shareholder activism has been homegrown and marked by strong activism at the retail level – in particular, small shareholders relying on mechanisms in the Corporations Act to provide them with a platform to agitate for social or environmental change (see above).

However, American-style hedge fund activism has become increasingly prominent in the Australian market. As well as Elliott Management's very public campaign against BHP, launched in April 2017, there are a number of other activists in the region that have been generating significant media attention – including value campaigns targeting Australian firms launched by Lone Star Value Management, Janchor Partners, Coliseum Capital Management and Elliott Management, and short campaigns against Australian companies launched by firms such as Glaucus and Viceroy Research.

The emergence of offshore shareholder activists with access to larger pools of capital has resulted in a broader range of targets for activist campaigns. A few years ago, the vast majority of activist campaigns against Australian companies were waged against small-cap companies. However, recent campaigns have targeted much larger companies, such as BHP (BHP Group Limited market cap: A$121.6 billion; BHP Group Plc market cap: £41.3 billion), Iluka Resources (market cap: A$4.5 billion) and Aveo (market cap: A$1.2 billion).[7] This trend is expected to increase as offshore investors gain confidence and become more active in the region.

iii Continued strength of strategic campaigns by local activists

Despite their recent increased prominence, hedge fund activism and other forms of economic activism are not new phenomena in Australia. Activist Insight data suggests that there was a 10 per cent increase in 60 Australian listed companies facing activist board-related demand in the 12 months ending 5 April 2019 (as compared with the prior corresponding period).[8] Activist shareholders, such as Sir Ron Brierley and Dr Gary Weiss, have been in the market for decades through various investment vehicles, and prominent local activist shareholders include Allan Gray, Mercantile Investment (which is Brierley-linked), Merlon Capital, Ariadne (which is Weiss-linked), MH Carnegie, Sandon Capital, Thorney Opportunities, and the local branches of Lazard Asset Management and Aberdeen Asset Management.

Activist campaigns by local investors continue to be very effective, reflecting local market knowledge and an ability to swiftly seize strategic opportunities. In line with the overall trend for offshore activists, it appears momentum is continuing and, indeed, increasing with recent campaigns from onshore funds, such as Merlon (in relation to financial services institution AMP), Sandon Capital (in relation to Watpac, Iluka Resources and BlueScope Steel) and Perpetual (in relation to Brickworks).

iv Characteristics of shareholder activist campaigns in Australia

Similar to the United States and the United Kingdom, hedge fund or economic activists operating in Australia typically seek to make an economic gain on an investment (usually in the short term) through means that are not aligned with the current strategy of the company. Common activist goals include the following:

a persuading companies to make a capital return or pay a special dividend;
b changing the business strategy (which the activist may seek to effect through a change in management or board composition);
c restructuring or selling a significant asset; or
d putting the company 'in play' or seeking to extract a higher price in a change of control situation.

7 Market capitalisations presented as at 8 July 2019.
8 Activist Insight, 9 April 2019.

Some activists may also 'bet against' companies that they perceive to be overvalued, looking to encourage a downward correction in the share price so they can close out a short position at a profit.

Though opportunities are most often identified by shareholder activists based on their own investment theses and research, in some cases they may be the result of institutional shareholders making a 'request for intervention'. Requests for intervention are most often made in respect of Australian companies with high levels of passive ownership through superannuation and pension funds, given those investors are often prevented from effecting changes at their portfolio companies themselves owing to resourcing and reputational considerations.

Until recently, the vast majority of activist campaigns in Australia have been conducted 'behind closed doors', with private approaches made by shareholder activists to companies' boards. Where the activist holds a significant stake, or is aligned with the board and management on a particular issue, it is common for the board to reach an understanding or negotiated outcome with the shareholder, in which case the matter would not usually become public. Often, at this stage, the activist would privately engage with members of the investment community (institutional shareholders, other significant investors and analysts) to build momentum for change and increase pressure on the company's board.

In Australia, it has historically been rare for shareholder activists to take the next step of publicly advocating for their proposed course of action (e.g., through white papers, open letters to the board, their own website or the media). However, recent activist campaigns have borrowed more heavily from the American hedge fund activist playbook, with tactics including the following:

a publicly criticising the board, individual directors and management;
b forming informal investor alliances and voting blocs;
c proposing or supporting candidates for appointment to the board;
d advocating for (or formally proposing) removal of existing directors;
e requisitioning shareholder resolutions and members' statements;
f requisitioning extraordinary general meetings of shareholders; and
g encouraging unsolicited offers for the company or its assets.

v Limitations on collaboration by shareholder activists

Under the Corporations Act, investors may become 'associates' for takeover and substantial holding notice purposes where they act together in relation to a common portfolio company. This provides an important protection for Australian companies in respect of the 'wolf pack'-type tactics sometimes seen in the United States, as it prevents shareholder activists from taking control of a company if other shareholders are uninformed about this passing of control and are not given any opportunity to obtain a control premium (or other benefits that would be paid if control were to pass legitimately).

Under the Corporations Act, an investor can become an associate of another investor if they propose to:

a enter into, or have already entered into, a relevant agreement with the other investor for the purpose of controlling or influencing the composition of the entity's board or the conduct of the entity's affairs; or
b act, or are acting, in concert in relation to the entity's affairs.

As stated by the Australian Securities and Investments Commission (ASIC) in regulatory guidance,[9] investors concerned about common issues may become associates or be regarded as having entered into a relevant agreement for the purposes of the takeover or substantial holding provisions. This is because these provisions are not only concerned with the power of individual investors in relation to the voting and disposal of shares in companies, but also the aggregated voting power of groups of investors who are either related or associated with each other in relation to some aspect of the entity's affairs. Depending on the aggregated voting power of the group, investors acting collectively in this way may be required to lodge substantial holding notices relating to the group, be prohibited from acquiring further interests in the entity under the takeover prohibition in Section 606 of the Corporations Act or even breach the takeover provisions.

The regulatory guide also clarified the circumstances in which investors acting collectively will and will not be taken to be associates for the purposes of the takeover and substantial holding notice provisions of the Corporations Act. Conduct that is permissible and unlikely to cause issues includes holding discussions with other investors, making recommendations to other investors in relation to voting, and making individual or joint representations to the company's board. Conduct that is likely to raise issues with associateship includes jointly signing requisitions for shareholders' meetings or resolutions, formulating joint proposals in relation to board appointments or strategic issues, accepting inducements to vote or act in a specific way, agreeing on a plan concerning voting or limiting their freedom to vote (e.g., by granting another investor their irrevocable proxy).

Another aspect that is unique to Australian law, especially relative to the United States, that renders wolf pack tactics high-risk is the country's broad insider trading rules that apply in relation to trading while in receipt of any material information in respect of a company (irrespective of whether it was sourced from a company insider). Prohibitions on 'tipping' similarly apply in relation to any material information regardless of its source. Knowledge of an activist hedge fund's intent to target a company on governance grounds could, in the context of a clear track record of being able to force a significant corporate transaction, constitute materially price sensitive information.

IV RECENT SHAREHOLDER ACTIVISM CAMPAIGNS

i AMP

Following criticisms levelled against it by the Financial Services Royal Commission, financial services institution AMP had a high level of turnover of key personnel in 2018 and 2019 and sought to undertake a 12-month portfolio review with a view to re-aligning the business with its core wealth management operations. The portfolio review culminated in the sale of AMP's life insurance business to British-based Resolution Life for A$3.45 billion, announced in October 2018.

The sale of AMP's life insurance business proved to be contentious with several of AMP's institutional shareholders who were critical of the price achieved and aggrieved that the company had not voluntarily sought shareholder approval for the sale. In the lead up to AMP's 2019 AGM, there was continued vocal opposition in relation to the sale and there was speculation that activist shareholders were planning to protest against the re-election

9 ASIC, *Regulatory Guide 128: Collective action by investors* (June 2015), [7]–[8].

of several of AMP's directors in relation to both the sale and the overarching turbulence at the company over the previous 12 months. During the campaign, AMP emphasised the company understood investors' frustration over the drop in AMP's share price and reassured investors that the right decisions were being made to put the business on a stronger footing.

Ultimately, AMP's shareholder engagement and reassurance was successful, with two influential proxy firms, Ownership Matters and CGI Glass Lewis, recommending shareholders support the re-election of all directors. At the AGM, resolutions concerning the company's remuneration report and re-election of its directors passed comfortably. AMP also avoided a second strike on its remuneration report and no resolution for shareholders to vote on a board spill was therefore triggered.

ii National Australia Bank

Similar to the other 'Big Four' Australian banks, National Australia Bank (NAB) was thrust into the spotlight by the Financial Services Royal Commission in relation to executive accountability for its risk and compliance outcomes, and the extent to which they were reflected in the bank's executive remuneration structure. In this context, NAB announced a new remuneration scheme, which sought to combine short and long-term incentives and included a 15 per cent pay reduction for executives.

The new remuneration scheme was not well-received by NAB shareholders and, at their 2018 AGM, NAB received its first strike against its remuneration report with 88.43 per cent of shareholders voting against the resolution. To date, this is the largest vote received by an ASX 300 company against a remuneration report in Australia. Particular criticism from investors included that the combined short and long-term incentive structure over-emphasised short-term performance and that, in the context of the criticism against NAB at the Financial Services Royal Commission, the proposed reductions to pay and incentives were not adequate.

Reflecting on the result, NAB announced that it understood shareholders' feedback and would redesign the remuneration scheme to better reflect stakeholder expectations and ensure it provides the right balance of financial metrics, customer outcomes and the management of non-financial risks over the long and short-term.

Apart from NAB, other banks that received strikes on their remuneration reports at their most recent AGM included ANZ and Westpac.

iii Woolworths

In the lead-up to Woolworths' 2018 AGM, the ACCR and the Labour Union Co-operative Retirement Fund assisted over 100 shareholders to requisition a two-limbed resolution that proposed to amend the company's constitution to allow shareholders to requisition advisory resolutions and then, in turn, requisition a resolution requesting the board to reach an agreement with the National Union of Workers to implement a labour hire providers' pre-qualification programme directed at their compliance with labour and human rights standards. The object of the resolution was ostensibly to ensure that Woolworths fulfilled commitments made prior to its 2017 AGM, in response to a similar requisitioned resolution also put by the ACCR. Two other resolutions were also requisitioned, which related to trade union involvement in worker rights education activities and grievance resolution procedures, and ongoing disclosure to shareholders about the company's domestic fresh food supply chain.

Woolworths responded to the requisitioned resolution by outlining the considerable steps it had taken to better understand and manage labour and human rights risks in its

supply chain, and recommending that Woolworths shareholders vote against the two-limbed resolution. Ultimately, the constitutional amendment resolution was overwhelmingly defeated (with 94.21 per cent of votes against it) and so the labour hire compliance programme resolution was not put to the meeting (though it had support of 14.92 per cent of the proxies submitted in advance of the meeting). In the chair's address, Woolworths reiterated it is committed to putting in place the right protections for workers within its supply chains.

V REGULATORY DEVELOPMENTS

i Fourth edition of the Corporate Governance Principles and Recommendations

On 27 February 2019, the ASX Corporate Governance Council released the final version of its fourth edition of the Corporate Governance Principles and Recommendations (the Fourth Edition Principles). The Fourth Edition Principles are planned to come into effect for listed entities' first full financial year commencing on or after 1 January 2020. There are a number of aspects of the Fourth Edition Principles that have the potential to catalyse further activism against ASX-listed companies, including a recommendation for ASX 300 entities to have a target of at least 30 per cent of directors of each gender on their boards and additional commentary on the disclosure of material exposure to environmental or social risks by companies (including a statement that companies that believe that they do not have such exposure are now expected to benchmark their disclosure practices against those of their peers and entities that do have such exposure are encouraged to consider implementing the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures). The recalibrating of expectations on social and environment practices under the Principles, including the enhanced disclosure that is expected to become typical market practice, is likely to catalyse continued activism in relation to these issues.

ii Modern slavery legislation

In 2017, the Joint Standing Committee on Foreign Affairs, Defence and Trade conducted an inquiry on enacting modern slavery legislation in Australia. On 29 November 2018, the Modern Slavery Bill 2018 (Cth) was passed by the Australian parliament and on 1 January 2019 the Act commenced. Among other things, the regime requires organisations with annual consolidated revenue of at least A$100 million to publish an annual modern slavery statement that contains information about the modern slavery risks in their supply chains, and their due diligence and remediation processes to assess and address those risks. Companies will prepare their first modern slavery statements in respect of their first full financial year commencing after 1 January 2019 (with six months to prepare and file the report).

In parallel, in June 2018, the Modern Slavery Act 2018 (NSW) (the NSW Act) was passed by the New South Wales parliament. The NSW Act provides for a similar obligation for commercial organisations with an annual turnover of A$50 million or more to prepare a modern slavery statement on the steps taken to ensure that their goods and services are not produced in supply chains in which modern slavery is taking place. The NSW Act also provides for the creation of a publicly available register that identifies organisations whose goods or services are or may be produced in supply chains in which modern slavery is or may be taking place.

Although the federal legislation is now in effect, the NSW Act is not. The relevant minister has indicated that the NSW Act will be referred to a parliamentary committee where it will be reconsidered, which may result in further amendments.

The modern slavery legislation in the form proposed by the federal and New South Wales governments will improve reporting standards in relation to human rights risks, which is a current area of focus for shareholder activists, as demonstrated by the ACCR's campaign against Woolworths. At this stage, it is unclear whether the increased disclosure on these issues will take the heat out of related activism or whether the transparency will prompt the targeting of slow adopters for activist action.

iii Introduction of a bill providing access to shareholders' email addresses

On 14 June 2017, former Senator Nick Xenophon introduced a bill into Parliament to amend the Corporations Act to require companies' registers of shareholders to include email addresses for each shareholder. At present, only shareholders' names, physical addresses and shareholding information form part of the register.

The Bill has still not been passed almost two years on, and there are no indications to suggest that it will become law in the foreseeable future.

VI OUTLOOK

As outlined above, the Australian regulatory regime is facilitative to shareholder activism and an increasing number of companies are being targeted by activist campaigns, particularly in relation to ESG matters. We expect that these trends will continue in the future given the current focus on corporate accountability in Australia and the continued public dialogue regarding social responsibility and ESG stewardship.

In relation to economic activism, offshore activists will continue to disrupt the traditional practice of behind closed doors activism in Australia, and a lack of responsive reaction by boards to private approaches will increasingly be met with more overt aggression and publicly hostile campaigns. However, most Australian boards have recognised the importance of strategic preparation, self-assessment and challenge as the most effective approaches to pre-empting and responding to activist campaigns.

The trend towards greater collaboration and engagement between traditionally passive superannuation long-term investors and activist funds is expected to continue. Partially offsetting that trend will be the support and acceptance of BlackRock's calls for greater focus on long-term value creation and its tempering of support for overt activist tactics marked by short-termism.

Appendix 1

ABOUT THE AUTHORS

QUENTIN DIGBY

Herbert Smith Freehills

Quentin Digby is a partner at Herbert Smith Freehills' Sydney corporate practice and established the firm's head office advisory team (HOAT) in 1998. HOAT specialises in strategic corporate governance issues, including board reporting and advice, market disclosure (both continuous and periodic), director and executive appointments, remuneration and disclosure, and shareholder communications and relations.

HOAT has established an unparalleled reputation for providing focused advice and guidance on not only legal and regulatory requirements but also market practice and emerging trends. HOAT advises the majority of the ASX 20 on corporate governance issues and is the principal governance adviser to approximately one-third of ASX 100 companies.

Quentin acts as a trusted adviser for the corporate secretariat, and general counsel teams and boards of a number of the firm's significant ASX-listed clients, and is the delegate for the Law Council of Australia on the ASX Corporate Governance Council.

TIMOTHY STUTT

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Timothy Stutt is a senior associate at Herbert Smith Freehills' head office advisory team (HOAT), where he advises publicly listed companies on corporations law, governance, executive remuneration, and shareholder engagement and activism matters. Timothy also has previous experience in the financial industry, having worked as an analyst for an investment manager based in the San Francisco Bay Area.

As a senior member of HOAT, Timothy advises ASX-listed companies on market disclosure and shareholder engagement issues, including in relation to sales downgrades, contentious general meetings, environmental, social and governance issues, economic shareholder activism and proxy adviser engagement. Timothy is a regular presenter on governance and remuneration matters for clients and at industry seminars (including at the Governance Institute of Australia).

In 2010, Timothy was one of two Australians to receive a Young Leaders Program scholarship from the Japanese Ministry of Education to study for his master's in business administration in Tokyo. He also holds a Bachelor of Laws (Hons.) and a Bachelor of Commerce from Monash University, Melbourne.

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