THE SHAREHOLDER RIGHTS AND ACTIVISM REVIEW

Third Edition

Editor
Francis J Aquila

THE LAWREVIEWS

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PREFACE

Over the years since the financial crisis, shareholder activism has been on the rise around the world. Increasingly institutional shareholders are taking a 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 has become a prominent, and likely permanent, feature of the corporate landscape. Boards of directors, management and the markets have increasingly become more attuned to shareholder activism, and engaging with investors is a priority for boards and management as a hallmark of basic good governance.

Shareholder activism is now a global phenomenon that is effecting change to the corporate landscape not only in North America but also in Europe, Australia and Asia. While shareholder activism is still most prevalent in North America, and particularly in the United States, shareholder activism continues to expand its reach across the globe. 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, 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 third 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 2018

Chapter 1

AUSTRALIA

Quentin Digby and Timothy Stutt[1]

I OVERVIEW

While 2017 heralded the emergence of American hedge fund activists in the Australian market, with Elliott Associates and Elliott International's (the Elliott Funds) campaign against global miner BHP, the first half of 2018 has again been marked by smaller scale activist campaigns, albeit in significantly higher numbers. The number of campaigns targeting companies headquartered in Australia rose a third in the first half of 2018, with a total of 41 campaigns commenced.[2] There was an increased focus on short selling-style campaigns, including a prominent campaign against Blue Sky Alternative Investments (Blue Sky) by American short-seller Glaucus Research Group (Glaucus), which generated high levels of media attention. The Glaucus campaign at Blue Sky came off the back of a successful short campaign against Australian sandalwood-grower Quintis (now in external administration). Overall, throughout 2018, the issues targeted by shareholder activists were rich and varied, including alleged financial mismanagement, criticism of positions taken in relation to takeovers and human rights and environmental concerns. Of particular note was Ariadne Australia's (Ariadne) successful campaign for representation on the board of Ardent Leisure, which saw Ariadne's Dr Gary Weiss assume the role of chair at Ardent Leisure.

Shareholder activism has long been a feature of the Australian corporate landscape, and it is not anticipated to retreat. Australia's shareholder-friendly regulatory regime has supported a robust, and increasing, level of engagement between the country's listed companies and their shareholders over economic, social and governance issues, and this trend is expected to continue for the foreseeable future.

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 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

1 Quentin Digby is a partner and Timothy Stutt is a senior associate in the head office advisory team at Herbert Smith Freehills. The authors would also like to acknowledge the assistance of Barry Wang, a solicitor in the Sydney corporate practice of Herbert Smith Freehills.

2 Activist Insight, 22 June 2018.

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 for the purposes of gathering 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 their 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 below in Section V for further details).

It is an offence to use information about a person listed in the register to contact or send material to them, 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.

In Australia, 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, such 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 and 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 for the purposes of formally considering and

voting 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 compulsorily 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). The shareholder is entitled to request that a statement be included with the notice of meeting setting out its 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 shareholder would be requisitioning the meeting, almost without exception the company's chairman 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 chairman 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), 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 need not give notice of the resolution if it is more than 1,000 words long or defamatory. However, it is otherwise required 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 continuing to increase, 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, in order 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). While this position was recently confirmed by the Full Court of the Federal Court of Australia,[3] the Australian Council of Superannuation Investors (ACSI) recently commissioned a report proposing that requisitioned resolutions in the form of non-binding advisory resolutions should be permitted (see further below in Section V).

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 that which would be otherwise 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.

The external candidate will typically be elected if they secure a simple majority of votes cast at the shareholders' meeting, unless the company is at its constitutionally mandated

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

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]

In order 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 above). 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 annual general meeting 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 annual general meeting and, in recent years, this mechanism has been co-opted by some activist shareholders as a 'protest' 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 (better known in Australia as 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 proceeding rarely proceed to trial in Australia, hostile shareholder activists will occasionally put the company on the notice they are contemplating such proceedings as a means of 'encouraging' the swift resolution of issues under negotiation. In some cases, proceedings may be instituted;

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 recent case of *RBC Investor Services Australia Nominees Pty Limited v. Brickworks Limited* [2017] FCA 756.

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:

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 sending 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 for the purposes of making 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.

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

However, depending on the intensity of 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 prominence of overseas 'economic' activists in 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. Even against a backdrop of falling attendances at annual general meetings in Australia, this form of small shareholder activism has continued to thrive and indeed grow, with many of the country's most prominent companies receiving director nominations from external candidates (e.g., Macquarie, BHP, Fairfax, Woolworths, Commonwealth Bank of Australia and Ten Network Holdings) or requisitioned resolutions from retail shareholders (e.g., Santos and Commonwealth Bank of Australia).

However, American-style hedge fund activism has become increasingly prominent in the Australian market. As well as the Elliott Funds' 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 the Elliott Funds and short campaigns against Australian companies launched by 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. During the period from 2013 to 2016, the vast majority of activist campaigns against Australian companies were waged against small-cap companies, with as few as 9 per cent of targets being large or mid-cap companies.[7] However, recent campaigns have targeted much larger companies, such as BHP (BHP Billiton Limited market cap: A$107.24 billion; BHP Billiton Plc market cap: £37.6 billion), Bluescope Steel (market cap: A$10.1 billion), Iluka Resources (market cap: A$4.9 billion), and Brickworks (market cap: A$2.37 billion).[8] This trend is expected to increase as offshore investors gain confidence and become more active in the region.

ii 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 at least 60 Australian listed companies each year have received a public demand from investors during the period from 2014 to 2017.[9] 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

7 Activist Insight (in collaboration with Arnold Bloch Leibler), 'Shareholder activism in Australia: a review of trends in activist investing' (30 June 2016).

8 Market capitalisations presented as at 7 June 2018.

9 Activist Insight, 22 June 2018.

is Brierley-linked), Ariadne (which is Weiss-linked), MH Carnegie, Sandon Capital, Thorney Opportunities and the local branches of Lazard Asset Management and Aberdeen Asset Management.

As evidenced by the Ariadne campaign at Ardent Leisure described in further detail in Section IV, 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 Sandon Capital (in relation to Watpac, Iluka Resources and BlueScope Steel), as well as regional funds, such as Janchor Partners (in relation to Vocus Group, Bellamy's Australia and, reputedly, Medibank Private).

iii Characteristics of shareholder activist campaigns in Australia

Similar to the United States and 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:

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

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.

While 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) for the purpose of building momentum for change and increasing 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 and the media). However, recent activist campaigns have borrowed more heavily from the American hedge fund activist playbook, with tactics including:

a public criticism of the board, individual directors and management;
b formation of 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.

iv 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 in circumstances where 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), 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, may be prohibited from acquiring further interests in the entity under the takeover prohibition in Section 606 of the Corporations Act, or may even breach the takeover provisions.[10]

In June 2015, ASIC released a regulatory guide to clarify 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.[11] Conduct with 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

10 Australian Securities and Investments Commission, Regulatory Guide 128: Collective action by investors (June 2015), [7]–[8].

11 Australian Securities and Investments Commission; see footnote 9.

associateship includes jointly signing requisitions for shareholders' meetings or resolutions, formulation of 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 are 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 or not). 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 Ardent Leisure and Ariadne

In a campaign that has been described as 'the largest successful activist campaign in Australia for decades',[12] Ariadne's Dr Gary Weiss became Ardent Leisure's Chairman in September 2017 following a successful campaign for election to the board, along with another Ariadne nominee, a month earlier.

Ardent Leisure became the subject of intense media attention after an accident at Dreamworld theme park in 2016 in which a faulty ride caused the death of four visitors. The period that followed saw the temporary closure of the park and a significant decrease in the company's share price. Growing concerns about the performance of the board led Ariadne, a minority shareholder with an approximately 10 per cent interest in the company, to commence a campaign to gain board representation. During the campaign, Ariadne emphasised that it was aligned with the interests of other shareholders given its significant stake and garnered further support by engaging a proxy solicitation firm, establishing a dedicated campaign website and distributing pre-populated proxy forms.

The chairman of Ardent Leisure's incumbent board initially resisted the campaign and refused to work collaboratively with Dr Weiss and the other Ariadne nominee. However, a few months later, when it had become apparent that the two Ariadne candidates were likely to be successfully elected at an extraordinary general meeting requisitioned by Ariadne, the campaign was effectively settled by cancellation of the shareholder meeting with the two Ariadne nominees, Dr Weiss and Mr Richmond, being invited to join the board. One month later, Dr Weiss was elected chairman of the board.

ii Myer and Premier Investments

Premier Investments, Myer's largest shareholder (which acquired a 10.77 per cent stake in the company in March 2017), has been engaged in a campaign for the replacement of the Myer board over concerns about the department store's continued decline in revenue, and share price.

12 Australian Financial Review, 'Ardent Leisure's capitulation the biggest win by activist investors in decades' (4 September 2017).

In October 2017, Premier Investments' proposal for the appointment of nominee directors and an additional director independent of Premier Investments to the Myer board was rejected. In response, Premier Investments voted against the resolutions proposed at the company's 2017 AGM, including the remuneration report, and encouraged other shareholders to do so. As a result, Myer received a 'first strike' against its remuneration report, representing an 'against' vote of more than 25 per cent. A second 'strike' at Myer's 2018 AGM would trigger a resolution for shareholders to vote on a board spill.

The Premier Investments campaign has continued in 2018 with increasingly strident shareholder communications and, in February, Premier Investments offered to collaborate with other shareholders to propose potential candidates for a new board (with the intention that if sufficient support from the institutional investors was obtained, the new board would be put to all shareholders at an extraordinary general meeting convened by Premier Investments). The process of engaging with the other shareholders is still ongoing, as confirmed in a letter to the other shareholders in May in which Premier Investments again encouraged them to hold the board to account.

iii Watpac and Sandon Capital

In February 2018, Watpac's largest shareholder, BESIX, proposed a proportional takeover of the company via a scheme of arrangement under which it would acquire half of the shares that it did not already own, thereby increasing its interest from 28 per cent to a controlling interest. BESIX offered shareholders 92 cents per share, which represented a premium of approximately 40 per cent.

While Watpac's independent board committee members recommended that shareholders vote in favour of the scheme of arrangement, Sandon Capital, an activist shareholder (which held a 3 per cent interest in Watpac), opposed the proposal on the basis that it undervalued the company and would give BESIX a majority shareholding to the detriment of the minority shareholders.

Sandon Capital's campaign received the support of proxy adviser Institutional Shareholder Services, which echoed Sandon Capital's concerns. The campaign was successful, with only 67.24 per cent of the votes cast at the scheme meeting in June 2018 being in favour of the proposed scheme of arrangement, which was below the requisite 75 per cent threshold.

iv Woolworths and the ACCR

In the lead-up to Woolworths' 2017 AGM, the ACCR assisted over 100 shareholders to requisition a resolution that would require the board to annually publish on the company's website a report on the company's due diligence process for identifying, analysing and addressing potential and actual adverse human rights impacts throughout its operations and supply chains.

On the day before the AGM, Woolworths announced that it had reached an agreement with the National Union of Workers on the implementation of a programme to identify and address human rights risks in its fresh food supply chains in Australia. Woolworths also committed to supporting workers in its supply chains to be educated about their workplace rights, have access to an effective grievance mechanism and be protected if they blow the whistle on human rights violations. As a result, the resolution was withdrawn by the ACCR.

v Environmental campaigns

In August 2017, certain shareholders of the Commonwealth Bank of Australia requisitioned a resolution to be considered at its annual general meeting that would require the directors to ensure that the company's business is managed in a manner consistent with the objective of limiting global warming to 2°C above pre-industrial levels. The resolution was not supported by the board and received only 2.94 per cent support.

In the lead up to Origin's AGM in October 2017, a series of resolutions were requisitioned that would require the company to provide information about its exposure to climate change-related risks, plan for transitioning to low-carbon technologies, and strategy for measuring and reducing short-lived climate pollutants. The resolutions were not carried as their validity was dependent on the adoption of a constitutional amendment that failed to pass.

A similar campaign was organised by the shareholders of Rio Tinto in 2018. A resolution was requisitioned for the company's AGM that called on the board to commission a review of the company's climate change advocacy practices through its participation in relevant industry associations (such as the Minerals Council of Australia, which has maintained a strong pro-coal stance). While the campaign failed for the same reason as the Origin campaign, the proposed resolution received 18.03 per cent support, which has been described as the highest vote ever in favour of a shareholder-requisitioned resolution on environmental issues in Australian corporate history.[13]

V REGULATORY DEVELOPMENTS

i Proposal to allow non-binding shareholder-requisitioned resolutions

In the past quarter of 2017, ACSI released a report supporting the use of non-binding shareholder resolutions and calling for changes to allow shareholders to requisition resolutions of this type. ACSI's recommended approach was developed in response to concerns raised by proponents of ESG activist campaigns that the courts' application of the current provisions of the Corporations Act essentially required a requisitioned resolution to be combined with an amendment to the company's constitution. The report galvanised significant debate but little consensus as to whether the reforms were necessary or appropriate.

ii Fourth Edition of the Corporate Governance Principles and Recommendations

On 2 May 2018, the ASX Corporate Governance Council released a consultation draft of the Fourth Edition of the Corporate Governance Principles and Recommendations (the Fourth Edition). As at the time of writing, the Fourth Edition is planned to come into effect on 1 July 2019. There are a number of aspects of the proposed Principles that have the potential to catalyse further activism against ASX-listed companies, including a recommendation for ASX300 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

13 *Sydney Morning Herald*, 'Rio Tinto delivers strong defence of its climate change stance' (2 May 2018).

Financial Disclosures). The recalibrating of expectations on social and environment practices under the proposed principles, including the enhanced disclosure that is expected to become typical market practice, is likely to catalyse continued activism in relation to these issues.

iii 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 28 June 2018, the Modern Slavery Bill 2018 (Cth) was introduced in the House of Representatives. Among other things, the Bill requires organisations with annual consolidated revenue of greater than 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.

In parallel, in June 2018, the Modern Slavery Act 2018 (NSW) was passed by the NSW parliament. The NSW legislation provides for a similar obligation for commercial organisations with an annual turnover of more than A$50 million 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 that use modern slavery.

The modern slavery legislation in the form proposed by the federal and NSW 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 if 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.

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

On 14 June 2017, 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 proposed Bill would provide persons requesting access to the register of shareholders, including activist shareholders, the means to electronically contact shareholders using their email addresses. Given the printing and postage costs involved in doing physical mail-outs to shareholders, the ability to contact shareholders by email is expected to provide shareholder activists with a significantly more cost-effective communications channel for activist campaigns.

The Senate Economics Legislation Committee reported on the Bill on 11 September 2017 but did not recommend in favour of it. As at the time of writing, the Bill had stalled before the Senate and was still awaiting its second reading.

VI OUTLOOK

As outlined above, the Australian regulatory regime is facilitative to shareholder activism and an increasing number of companies (in particular, an increasing number of larger companies) are being targeted by activist campaigns. We expect that these trends will continue in the future.

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 approach 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 their tempering of support for overtly activist tactics marked by short-termism.

Nevertheless, the increased use of shorting by some shareholder activists, including public 'short' campaigns against specific companies, is expected to continue in the near term given the prevailing low-growth environment, albeit with increasing regulatory scrutiny.

Appendix 1

ABOUT THE AUTHORS

QUENTIN DIGBY

Herbert Smith Freehills

Quentin is a partner in 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 now advises 60 per cent of the ASX 20 companies on corporate governance issues and approximately 40 per cent 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

Herbert Smith Freehills

Timothy is a senior associate in 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, ESG and 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 (MBA) in Tokyo. He also holds a Bachelor of Laws (Hons.) and Bachelor of Commerce from Monash University, Melbourne.

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