DOING THE TWO-STEP

An interview with Michael Verrechia, managing director in the M&A and Activism Advisory Group at Morrow Sodali.

HOW HAS THE PANDEMIC CHANGED M&A ACTIVISM?

MOST of the deals we have worked on recently have had some level of concern of shareholder activism or traditional public opposition. We have seen that opposition manifest in different forms, whether it's been a proxy contest with competing ballots, a formal "vote no" campaign supported by an activist's white paper, or simply rumors on the Street of alternative transactions that were not fully explored by a company's board. I expect the M&A arena will continue to be a focus for activists looking to squeeze additional value out of announced deals.

As a shareholder engagement and proxy solicitation firm, our main concern in the initial days of the pandemic centered around how we would effectively and directly communicate with the different shareholder constituencies. As we all saw, institutional investors easily pivoted to virtual meetings and Zoom. However, there was still concern surrounding reaching retail holders due to processing and mail delays. Those shareholders become critically important in close votes. In the end, while the mail system was incredibly behind in the onset of the shutdown, we did see a sizeable increase in retail holders willing to engage with us over the phone.

WHAT CAN A COMPANY DO WHEN SHAREHOLDERS OPPOSE AN ANNOUNCED DEAL?

As we all know, when an activist investor opposes an announced deal, it puts the shareholder engagement program and communication strategy into overdrive. Much of what needs to be discussed with shareholders revolves around the process of the target company accepting the announced deal as the "best" deal.

That said, in the past six months I have worked with opposing shareholders targeting transactions that did not result from a conflict-free sales process. One announced a transaction that did not receive unanimous support from the board of directors. Of course, at the end of the day, price ultimately drives the success of the vote and closing of the transaction; if shareholders believe they can squeeze additional value by publicly opposing the transaction, they may try to.

WHAT ARE SOME RED FLAGS THAT COULD INDICATE A DIFFICULT SOLICITATION?

Aside from immediate negative market reaction, a major warning sign is a rapidly changing shareholder base prior to a record date – the retail population can increase dramatically. Since the pandemic, we've seen this happen quite a bit in special purpose acquisition company (SPAC) deals. For some SPACs, the retail base can reach 25%-30% of the voting population which is problematic because retail holders are typically poor voters and require additional time for solicitation. In those situations, we have to be creative in deploying different strategies for maximizing the retail voting return. That means crafting an overall campaign that goes directly to the shareholders (letters, phone calls, multiple ballots) while also targeting potential voters through social media and advertising.

WHAT CAN COMPANIES DO WHEN AN ACTIVIST PUSHING FOR A SALE LAUNCHES A PROXY FIGHT?

In the past six months we have been involved in a few situations where an activist investor was looking at a two-step fight with the goal of reaching an announced deal with a higher premium. The first step is obviously to vote down the deal, with the second step being a contested election to secure representation on the board.

When a company finds itself in a proxy contest, either against a proposed deal or for board seats, it is critical to first understand the company's changing shareholder profile from a voting control perspective. Not only does a shareholder base significantly turn over post announcement of a transaction but companies typically rely on very stale public filings for information. Identifying current shareholders should be the basis for how the overall defense campaign should be run. From there, it is truly an exercise in defending your deal and why it is in the best interests of all shareholders. To that end, companies and boards should have a full team of advisers on tap who can prepare them to engage with shareholders and secure their votes.