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Client Alert

June 2017

Trap for the Unwary Shareholder Activist: The Latest Tactic by Companies to Tilt the Playing Field in Proxy Contests

Shareholder activists seeking to nominate director candidates for election to the boards of their portfolio companies are advised to be on the lookout for the latest trap for the unwary designed by company defense law firms to further entrench board members. The trap is embedded in questionnaires and representation agreements that are now commonly required to be submitted by a nominating shareholder's director nominees under nomination procedures contained in company bylaws. Taking the bait can give the company a significant strategic advantage over the dissident in an election contest.

Consent of Dissident Nominee to Be Named on Company Proxy

Shareholder activists familiar with the nomination process know that it is now common practice for companies to require a nominating shareholder's nominees to submit a questionnaire and representation agreement as part of the nomination submission. The questionnaires are typically similar to director and officer questionnaires companies use internally in order to obtain information from insiders required to be disclosed in their proxy statements and annual reports. The representation agreements typically require the dissident nominee to certify that such nominee will not have any undisclosed voting commitments with respect to his or her actions as a director, will not become a party to any agreement with any person other than the company with respect to compensation in connection with his or her service as a director, and will comply with the company's internal policies if elected.

We are beginning to see questionnaires and representation agreements seeking to obtain the written consent of dissident nominees to be named as nominees in the company's proxy materials. By way of example, the following item was buried in the last page of a 23-page questionnaire that the nominees of one of our activist clients were recently asked to complete:

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CONSENT TO SERVE.

If you are a nominee for director:

I hereby consent to being named as a nominee for Director in the current Proxy Statement of the Company and agree to serve as a Director of the Company if elected at the Company's current Annual Meeting of Stockholders.

Initial to indicate consent: _____

At first, we chalked this up to poor drafting by companies in re-purposing their existing forms of director and officer questionnaire for use as a nominee questionnaire since existing company directors are expected to consent to being named in the company's proxy statement. However, overzealous defense advisors are beginning to seize on this seemingly inadvertent drafting error in an attempt to get a leg up on the dissident by purporting to require shareholder nominees to consent to being named in the company's proxy.

Providing the written consent of a dissident nominee to be named as a nominee in the company's proxy materials could be extremely detrimental to the dissident's campaign as discussed in further detail below. It is therefore critical that any materials a nominating shareholder and its nominees are asked to sign by a target company as part of the nomination process be reviewed by counsel experienced in shareholder activism.

Tilting Strategic Landscape in Favor of Target Company

Under Rule 14a-4(d)(1) of the Securities Exchange Act of 1934, a proxy may not confer authority to vote for any person for election to the board unless that person has consented to be named in the proxy statement and to serve if elected. Under this provision, known as the "bona fide nominee rule," neither the company nor the dissident may include the other party's nominees on its proxy card without the nominee's consent. This consent is rarely provided by activists as allowing the company to include one or more of the dissident's nominees on its proxy card could give the company a significant strategic advantage in its solicitation. These strategic advantages include the following:

- If the company's proxy card gives shareholders the optionality to vote for its nominees as well as one or more of the dissident's nominees, shareholders who wish to mix and match their votes among all the candidates may be inclined to complete the company's proxy card instead of the dissident's card.

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- If a proxy advisory firm such as Institutional Shareholder Services (ISS) recommends that shareholders split their votes among the company's nominees and the dissident's nominees and the recommended dissident nominees also appear on the company's proxy card, the advisory firm may also recommend that the shareholders complete the company's proxy card (which gives the shareholders the optionality to vote for all its recommended nominees) instead of the dissident's card.

- If the company believes it is at a strategic disadvantage in the contest and that recommending and soliciting proxies for the election of one or more of the dissident's nominees could be advantageous to its campaign, it will be able to do so by naming the nominee(s) on its proxy card.

Engaged Capital vs Rent-A-Center

In Olshan client Engaged Capital's recently completed proxy contest at Rent-A-Center ("RCII"), Engaged Capital was forced to initiate litigation in the Delaware Court of Chancery to thwart any attempt by RCII to include Engaged Capital's nominees on its proxy card. RCII's nominee questionnaire and representation agreement each included a requirement that Engaged Capital's nominees consent to being named in RCII's proxy statement. In a cover letter to RCII accompanying the completed questionnaires, signed representation agreements and other nomination materials, Engaged Capital asserted that such a requirement was completely inappropriate as Engaged Capital would be filing its own proxy statement. Engaged Capital also noted that its nominees had clarified in the questionnaires and representation agreements that they consented to only being named in Engaged Capital's proxy statement.

After RCII asserted that Engaged Capital's nomination materials were deficient by virtue of the nominees' failure to consent to being named in RCII's proxy statement, Engaged Capital sent a second letter to RCII reiterating that it did not believe that RCII's organizational documents required Engaged Capital's nominees to consent to being named in RCII's proxy statement in order for their nominations to be valid or that it would be equitable for RCII to name Engaged Capital's nominees in its proxy statement.

In an abundance of caution and subject to a full reservation of rights, Engaged Capital delivered to RCII revised nomination materials that included the nominees' consent to being named in RCII's proxy statement. Shortly thereafter, Engaged Capital filed a lawsuit against RCII in the Delaware Court of Chancery seeking an order declaring Engaged Capital's original nomination materials to be valid and prohibiting RCII from including Engaged Capital's nominees in its proxy statement. After the

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court granted Engaged Capital's motion to expedite its action, RCII notified Engaged Capital that it would not be including Engaged Capital's nominees in its proxy materials – rendering the claim moot.

At the June 8 annual meeting, all three of Engaged Capital's nominees were elected to RCII's board in place of three long-standing incumbents, including RCII's Chairman and CEO. Had Engaged Capital not challenged RCII's ability to include Engaged Capital's nominees on its proxy card, the outcome of the election contest may have been different.

Marcato vs Buffalo Wild Wings

In the recently concluded election contest waged by Marcato Capital Management ("Marcato") against Buffalo Wild Wings ("BWLD"), both Marcato and BWLD included Sam Rovit, who was originally nominated by Marcato, in their respective slates of director nominees and Mr. Rovit was named on each of their respective proxy cards. According to public filings, after Marcato nominated its slate of directors, members of its slate, including Mr. Rovit, were interviewed by BWLD's governance committee to discuss their interest in serving on the board. BWLD subsequently announced that it had nominated Mr. Rovit. BWLD's proxy disclosure discussing its nomination of Mr. Rovit illustrates how a target company can use a highly qualified candidate put forward by a dissident as a strategic measure to bolster its own campaign:

> Notably, Mr. Rovit was initially nominated by Marcato and, after careful and deliberate evaluation by our Governance Committee, we believe Mr. Rovit will contribute to our Board.
>
> We therefore enthusiastically nominated him ourselves.

The circumstances surrounding the provision of a written consent BWLD would have been required to obtain from Mr. Rovit in order to name him on the company's proxy card are unclear from the disclosure contained in the proxy statements filed by both sides. BWLD's proxy statement suggests that Mr. Rovit had provided his written consent to be nominated by the company prior to the announcement of his nomination, stating:

> [The Chairman of the Board] spoke with Mr. Rovit by telephone and Mr. Rovit confirmed his prior written statements indicating his willingness to be nominated by the company for election to the Board of Directors.

However, according to Marcato's proxy statement, immediately after BWLD announced that it had nominated Mr. Rovit, BWLD requested that

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he sign a consent to be nominated by the company and to be named in its proxy statement and that such request was denied:

> After this announcement, the Company's general counsel . . . sent an email to Mr. Rovit asking him to sign a form of consent to being nominated by the Board for election at the 2017 Annual Meeting and to be named as such in the Company's proxy statement for the 2017 Annual Meeting and other proxy soliciting materials. Mr. Rovit did not sign such consent.

Nevertheless, in the days leading up to this announcement, Marcato was clearly concerned with the possibility that BWLD would nominate one or more of its nominees and the strategic advantage BWLD could gain in its solicitation if a subset of Marcato's nominees were named on the company's proxy card. One week prior to the announcement, Marcato counsel sent a letter to BWLD counsel expressing these concerns and suggesting that both sides agree to using a "universal" proxy card listing all candidates in order to level the playing field. BWLD rejected this proposal.

Subsequently, Mr. Rovit sent a letter to BWLD expressing similar concerns that his inclusion on the company's slate was a tactical measure intended to entrench the board and his view that both sides should agree to use a "universal" proxy card. Mr. Rovit stated:

> It is my understanding that the Company has rejected Marcato's proposal to use a proxy card that would provide shareholders the option to vote for each of the nominees proposed by Marcato or the Company, regardless of which proxy card is used. By excluding the other Marcato nominees from its proxy card, the Company has deprived shareholders of the ability to make a real choice in the upcoming director election. I therefore worry that my inclusion on the Company's proxy card is a tactic meant to help entrench the current board, and I would not appreciate my candidacy and name being used in that manner.

In its report recommending that shareholders vote for the election of Mr. Rovit, among other candidates, ISS echoed Marcato's concerns that BWLD's nomination of Mr. Rovit appeared to be tactical. ISS stated:

> Moreover, certain decisions, such as the company's inclusion of Marcato nominee Rovit on the management slate, come across as gamesmanship rather than a proactive assessment of the facts and circumstances.

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At the June 2 annual meeting, Mr. Rovit together with two of the other three Marcato nominees and six of the other eight BWLD nominees were elected to the board. We can only speculate as to the degree of impact BWLD's tactic had on the results of the election contest.

* * * * *

Please contact the Olshan attorney with whom you regularly work or one of the attorneys listed below if you would like to discuss further or have questions.

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