CORPORATE GOVERNANCE CAUSES FOR SHAREHOLDER ACTIVISM

As shareholder interests have become more diverse, and costs of fighting activist shareholders grow, companies have sought to both limit shareholder activism and decrease its visibility. Recent research in *Strategic Management Journal* explores the conditions under which firms will be targeted for both visible activism (proposals on company proxies) and private activism (proposals resolved through negotiation between the shareholder and management).

Key Takeaways:

- Activist shareholder proposals are more common for firms with higher CEO pay and CEOs serving as board chair, and less common for firms with larger boards and more institutional ownership.
- Successful private negotiations with activist shareholders are more likely for firms with CEO ownership, lower CEO pay, smaller boards, and less institutional ownership.

Focusing on S&P 500 firms over a 6 year period, the researchers examine the effects of corporate governance on shareholder activism. Visible activism is more likely when CEO compensation is greater, CEOs serve as board chair, and the company's largest shareholder owns a greater percentage, while it is less likely when the board has more directors and there is greater total institutional ownership. Larger, poorly performing firms with higher book to market ratios are also targets for visible activism. At the same time, companies are more likely to successfully negotiate privately with activist shareholders when CEO compensation is lower, CEO ownership is higher, there are fewer directors on the board, and there is less total institutional ownership. Successful private negotiation is also more likely for smaller firms, higher performers, and those with lower market to book ratios. Interestingly, the percentage of independent, outside directors on the board does not affect visible or private shareholder activism.

In short, corporate governance strongly relates to shareholder activism; however, mechanisms designed to align incentives of management with shareholders are far more successful in limiting activism than mechanisms associated primarily with monitoring. Further, understanding the causes of both visible and private activism can be important to identify how companies choose to deal with potential activists.

Source: Goranova, M., Abouk, R., Nystrom, P.C., & Soofi, E.S. (2016). Corporate Governance Antecedents to Shareholder Activism: A Zero-Inflated Process. *Strategic Management Journal*, DOI: 10.1002/smj.2472.