
PHOTOGRAPH: STEVEN LAXTON

Europe Courts MARTY LIPTON

Brunswick's **KEVIN HELLIKER** speaks with **MARTY LIPTON,** a legend in corporate battles against activists, about the latest trends in that war

FOR HALF A CENTURY MARTY LIPTON HAS been the defender of choice for companies under attack by an activist investor. That has been his specialty since he graduated from the New York University School of Law in 1955. The inventor of the "poison pill" strategy for thwarting hostile takeovers, he published a landmark article in 1979 on the responsibility of board members to stakeholders other than shareholders. A 1992 article he co-authored, "A modest proposal for improved corporate governance," became the template for basic corporate governance principles that were adopted in the 1990s.

Far from slowing down at 86, he has become an important adviser to lawyers and board members in Europe, where activism recently has taken root. From the Midtown New York offices of the law firm he founded in 1965, Wachtell, Lipton, Rosen & Katz, Lipton reiterated his long-standing arguments against activism, while noting that the battle has taken some recent turns. What follows are the thoughts he expressed in that interview along with select excerpts from previous conversations with Brunswick.

Have activists become an ordinary and less acrimonious part of the corporate landscape?
Yes and no. Certainly the acrimony has increased with activists like Paul Singer and Bill Ackman, and the number of activists has increased. Most institutional investors are not terribly affected by acrimony. But some of the activists feel that acrimony is essential to achieve their efforts. It's hard to generalize. There are 15 or so major activists and another 100 or so more. They have different targets and different strategies. Some activists who had a very aggressive strategy have changed and are much more cooperative. I think probably the single most significant development has been that some of the major activists have essentially shifted so they no longer promote

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financial engineering or short-term changes. Some are basically looking to invest to help a company change its strategy. Sometimes to improve it. And they've had quite a bit of success doing it. It's sort of like an old-fashioned merchant bank having a significant investment in a company and trying to help it on a long-term basis. I call them pro-bono management consultants.

Are boards open to that or resisting it?
The P&G board resisted it with Trian last year. But some boards have encouraged it or at least accepted it.

I'm guessing your advice would depend on the case?
Depends on the case. Unless a company is quite comfortable that it could win, it's usually a mistake to go into a proxy fight. Even if it's won, a close vote sets up a situation where any downturn, any problem, could result in a change of leadership. It's not helpful to management to have a proxy fight that comes out, even if you win it, you know, 52-48, something like that. That just shows that 48 percent of the shareholders are not satisfied with the way the company is being managed.

Unless a company is comfortable that it's going to win a proxy fight by a large margin, it should not undertake one. It's better to settle the matter and put one or two new directors on the board.

In other cases where the activist is promoting something that's untenable, or something the company feels runs contrary to the best interests of shareholders, then the company is basically forced to defend a proxy fight and should do so, but always keeping in mind that a close win is the equivalent of a loss.

The most important thing is that the company has a very good IR effort and a real understanding of what its principal shareholders are thinking. What is their evaluation of the company? What is their opinion of management? On the basis of that information, the company can make the right decision as to whether to settle or to fight.

Are you more often recommending that boards negotiate with activists?
Not really. About the same. I have one message: activism is a disaster for the economy. And unless that gets played back, we are condemning ourselves to low growth – or no growth.

Is demand for your and your firm's counsel as strong as ever?
I'd say it's as high as it's ever been, maybe even a little higher.

As activism spreads across Europe, is your counsel in demand there?
Europe hadn't experienced activism, and now there's a sharp increase in it not just in Europe but around the world. Publicly traded stocks on stock exchanges everywhere are subject to activism.
I would say the trajectory for activism outside the United States is at a higher rate than the growth of activism in the US.

While we don't operate in other countries, we've had a significant number of situations where companies outside the US have come to us for help in dealing with an activist situation in their country.

Do you advise by phone or travel to the scene of the battle?
Oh, we travel. An activist battle is basically fought on the home country's turf. You might give some advice long distance, but you basically have to be on the ground when you're in the midst of an activist fight. In dealing with an activist situation, there are a lot of people that need to be involved and it's always best to meet in person. It doesn't mean you stay there for a month or two. It's back and forth.

Does a strong market provide some coverage to companies that might otherwise become activist targets?
Yes. If the price of a stock has gone up, it improves the total shareholder return. One of the key metrics that activists use is comparison of the target's TSR to the peer group TSR. And to the extent that the target's TSR is lower than the peer group, it's an argument that activists like to use.

Some proponents of long-term investing, for instance McKinsey's Dominic Barton, have suggested that short-termism may play a role in rising populism. What do you think?
I view activism as being a major factor in inequality. And inequality always breeds populism. There are a number of economic studies that show that. There are organizations like the Coalition for Inclusive Capitalism that are trying to moderate short-termism and activism in order to make the economy more inclusive.

Going back to 1970, when Milton Friedman published an article in *The New York Times* basically saying that the sole social purpose of a corporation should be maximizing value for the shareholders – usually virtually those words – there's been academic support for short-termism and activism.

There are those who have accepted that and basically believe that shareholders should have absolute control over the corporation and that management should operate solely to maximize the return to shareholders.

I think it's axiomatic that if that thinking dominates an economy, the average worker is going to get less and the shareholders are going to get more. And sooner or later, you have created a degree of inequality – and really, despair – that's going to spur a sharp populous turn.

That's been true throughout history. Step back to Roman times. If there's an elite that begins to take an outsized share of the economy, it causes disruption and ultimately some kind of revolution. It can be a revolution that moves toward a more socialistic approach, or it can be a sharp turn to a totalitarian approach. But one way or another, the few who control the source of income in an economy, whether it be land in feudal times or business corporations in modern times, you're going to get a reaction unless there's a fair mediation of the proceeds of economic activity.

A series of economic studies, two of which have come from Europe, showed that activism – short-termism, shareholder-centric governance – is responsible for a very material drag on GDP growth in the US, UK, Netherlands, France and Germany. If companies don't invest, you're not going to get an increase in productivity, you're not going to create employment – you're not adding to the economy. It doesn't take statistics to show that. It's plain, ordinary common sense. And people are beginning to have common sense.

That's why I feel so strongly that activism is not beneficial to an economy and it should not be encouraged. Now, there are always companies that are not well-managed, pursuing a bad strategy. Those companies need to be turned around, but it is not necessary to have activists do it. The institutional investors should undertake to engage with those companies and convince them to turn around. If you promote activism, what you're doing is sending a message to every company that it should start thinking the way of the activist or otherwise it's going to be attacked, which means in a sense that you kill long-term strategies.

So what can be done?
We need to rethink corporate governance. The board of directors should determine the strategy of the company. We've taken that away and put the power into the hands of shareholders. The best way of dealing with that is for institutional investors to stop outsourcing the monitoring of their investments, and instead take it in-house.

What really annoys me, what I get really angry about, is that the public and union pension funds don't try to do something about this. Activism is the cause of these great layoffs. It is bad for working people, it's bad for shareholders and it's bad for the economy.

How should boards deal with the potential for activism?
What activists are trying to do is drive a wedge between the board and management. Boards need to be prepared to back the management. Boards need to be on top of shareholder relations, to be ready to meet with institutional investors. Then they will get the support of institutions to win proxy fights.

That means, with regard to the potential for activism, the single most important thing for a CEO is to maintain a relationship with the board of directors so the board doesn't feel pressured to seek a solution that's not in the best interests of the long-term shareholder.

How optimistic are you for future generations?
Well, at the moment one cannot be very optimistic because the world is somewhat chaotic, both from an economic standpoint and a political standpoint. And the failure of investment, both in business corporations and by government, has basically penalized future generations.

If you don't invest in infrastructure – and by infrastructure I mean not only bridges and roads but also soft infrastructure like education, employee training, healthcare and housing – if you don't invest in that, you're basically penalizing future generations. We've now had more than 16 years of robbing from future generations.

KEVIN HELLIKER, a Pulitzer Prize-winning journalist, is Editor-in-Chief of the *Brunswick Review*.

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MARTY LIPTON

A founder in 1965 of Wachtell, Lipton, Rosen & Katz, Marty Lipton is a dean of mergers and acquisition law, his practice focused in particular on corporate defense. He invented the so-called poison-pill defense.