# Open your mindset to the bigger picture

*For a better annual meeting… look beyond the annual meeting.* **By David Silverman**

In the wake of the financial crisis, the long-term trend of boards and management teams listening to the perspectives and ideas of their major shareholders has gathered new momentum. Boards are working harder in an environment of greater regulatory accountability, and more companies than ever are earnestly trying to take good governance seriously. Yet annual meetings remain emblematic of the limitations of the process-oriented approach to corporate governance to which most companies still adhere.

For the most part, companies still approach the annual meeting primarily as a requirement that must be satisfied, and secondarily as an employee communication event. For many companies the annual meeting is the only time during the year when they ostensibly discuss the board with their investors. Despite the fact that boards are generally more qualified, more engaged, and more knowledgeable about their companies than ever, the prevailing goal of most annual meetings — "bring it to closure" — harkens back to an era of unimpressive boards.

I believe companies should be marketing governance as a strength, emphasizing that shareholder capital has the right people and the right structure around it to provide long-term value. A bigger-picture approach to corporate governance by boards and their companies not only would benefit investors, it also could help address the common complaint among management teams over "short-termism" within the investment community.

As a long-term shareholder — Blue Harbour typically takes significant minority positions in companies that are open to our ideas for unlocking value, and we expect to hold our positions for a multi-year time period while companies execute their strategies — I believe the quality of the board and management and their willingness to promote transparency is absolutely critical. Over a three-year time horizon, any company's circumstances can and will change in unknowable ways, whether due to the economy, currency fluctuations, technological developments, new competitors or a host of other variables. So even more important than the quality and credibility of any particular set of assets or business strategy is the skill and experience of the board and management team that I'm relying on to regularly test and reassess the strategy and adjust it or overhaul it as changing conditions require.

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## Provide the tools

If companies want to attract long-term shareholders — the kind of shareholders who, for example, will support a temporary reduction in earnings for the betterment of long-term value, or stick with a company through a rough period and in so doing dampen stock volatility — they should provide the tools for understanding their long-term potential. No shareholder should expect a company to provide, for example, detailed five-year earnings projections for a new acquisition, but a long-term shareholder needs the tools: What are the com-

# How to fix the annual meeting … in 100 words or less

That was the challenge presented to a network of *Directors & Boards* colleagues and readers of the *e-Briefing* monthly newsletter. Here is a selection of responses.

**I would remove** the 'annual' — once a year isn't engagement. Have an annual polling session with statutory reports but have other interaction for meaningful exchange of ideas between those annual sessions. David Gonski, a well-respected Australian chairman, once reflected that an annual general meeting with shareholders was like a drunken one-night stand with some total strangers! I tend to agree — not that I have ever tried his analogy… it is just that I find the meetings so unfulfilling.

— ***Julie Garland McLellan,*** author of the new book *Presenting to Boards* and one of Australia's leading governance experts (www.mclellan.com.au)

**Fixing the annual meeting** begins with proper preparation in advance. Step 1: All directors should read every word of all publicly available documents in advance of the meeting with the intent of seeing the company through the eyes of its most knowledgeable outside stakeholders. Step 2: Directors should meet with shareholders and other stakeholders and prepare and present a report of findings at the meeting. Step 3: The board should prepare and present a report on how it has added value for all shareholders and stakeholders and its plans to improve its performance in future years.

— ***Eleanor Bloxham,*** CEO, The Value Alliance (www.thevaluealliance.com)

**The annual meeting should be** one of the company's main investor relations events of the year. It should be a showcase for the company's products, its culture, its strategic direction, and its corporate governance. In addition to a regular investment or marketing road show, presentation should be made as to various governance structures and activities the company's board has gone through during the year. Individual board committee chairs should get up and make the presentation of what his/her committee worked on during the year and their goals for the coming year. At a minimum, shareholder input should be solicited and, optimally, dialogue be had. If the above were to be conducted annually and investors could count on it, there would be a build-up of in-person and webcast attendance that would be worthwhile in terms of awareness and positive perception, which would find its way eventually in a higher stock price.

— ***Andrew Shapiro,*** president, Lawndale Capital Management LLC (www.lawndalecap.com)

**Shareholder governance pressure** will obviously continue during the 2011 proxy season as the Dodd-Frank Act interpretation by the SEC continues to become a reality. Meanwhile, in response, some companies are beginning to consider changing the annual meeting process to include both audit and compensation committee chairs offering planned comments during the meeting. The focus would be to provide a visual awareness of a chair and issues that have been considered by a committee.

— ***C. Warren Neel,*** corporate director and executive director of the Corporate Governance Center at the University of Tennessee (www.corpgovcenter.utk.edu)

**Almost all shareowner meetings** are too formal, perfunctory, and sanitized to be useful (apart from the real activities related to proxy voting). Although most likely only a partial fix, I think giving shareowners, and perhaps other non-owner stakeholders, the real ability to place items on the agenda for discussion and reaction by directors (who should be required to attend every AGM) would improve AGM effectiveness.

— ***Michael McCauley,*** senior officer, Investment Programs & Governance, Florida State Board of Administration (www.sbafla.com)

**Advance notice,** voting by proxy, shareowner dispersion and other factors reduced the meaningfulness of annual shareowner meetings. Yet, "face-to-face accountability" can still change corporate policy. Recent "virtual-only" meetings demonstrate they are not ready for prime time, just as tablet computers needed years of development prior to iPad success. "Hybrid" meetings provide a testing ground for security issues, intuitive interfaces, independent facilitators using published procedures, Q&A sessions around each proxy item and other experiments that can lead to increased accountability. Technology can facilitate real deliberation or devolution into meaningless ritual. The choice is ours.

— ***Glynn Holton,*** executive director, United States Proxy Exchange, and ***James McRitchie,*** publisher of CorpGov.net (http://CorpGov.net)

**The constraints are real:** limited time, limited participation of shareholders, and legal constraints on what can be said. Investors hoping to discern novel insights at the annual meeting are ripe for disappointment. So spend time on giving shareholders a window on how the board and management interact on an issue of substance. Dispense with serial presentations in favor of a less-scripted discussion of an unusually challenging risk or opportunity, with questions from shareholders online or in person. Bring corporate governance to life to validate shareowner confidence in the stewards of their interests.

— ***Matt Orsagh,*** CFA, director, Capital Markets Policy, CFA Institute (www.cfainstitute.org)

**How about letting** directors answer questions from shareholders? A rookie meeting attendee once asked me, "Why are the directors sitting at the front of the room with their backs to the shareholders? Shouldn't they be facing the shareholders?" The question was utterly guileless, but I didn't have an answer.

— ***Cornish Hitchcock,*** principal, Hitchcock Law Firm (www.hitchlaw.com) pany's acquisition criteria? How is compensation aligned with performance? What prior experience do the board members and management have in integrating and deriving value from acquisitions, and what are their track records?

## Not the only opportunity

Companies who desire long-term shareholders should view the annual meeting as one opportunity to showcase the strength of their boards, but by no means the only one. If a company wants to attract the kind of shareholder who cares about the long term, it should discuss governance issues at its annual investor day and other venues where it interacts with its investors, because governance informs quality decisions over the long term. It should strive to turn the proxy's compensation discussion and analysis section into a marketing communication that also accomplishes a legal requirement, as opposed to a legal requirement in and of itself. Explain to shareholders how the board and management are eating their own cooking via compensation that pays out only upon realization of the longer-term value creation.

*I believe companies should be marketing governance as a strength.*

Process-oriented, prescriptive approaches only go so far. When boards and managements reach further to adopt a "shareholder mindset," the big picture becomes clearer and they will find the tactical steps that make sense for their particular cases. ■

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## NIRI's suggested steps for a better experience

**By Jeff Morgan**

**Boardrooms throughout the country** are rapidly learning that one upshot of Dodd-Frank is greater shareholder influence on corporate governance matters, including increased shareholder interest in communicating directly with boards. Factor in the loss of the broker vote in director elections (thanks to the NYSE Rule 452 amendment), and many companies and their directors are rightly concerned about simple, non-routine director elections.

These new rules serve to highlight the increasing importance of any public company's investor relations (IR) function. I believe that as the key link between the company and the investment community, boards of directors will of necessity rely more directly on IR for information and deeper insight into their shareholders in this new environment. And I believe that companies and boards should view this new environment as an opportunity to develop new and better methods for communicating with these shareholders.

One traditional corporate/shareholder communications opportunity that seems to have fallen on hard times is the annual meeting. Roundly criticized by all sides as an antiquated, ill-attended exercise in regulatory compliance, there are steps that companies and boards could take now to make the 2011 annual meeting a much better experience for all:

• *Change your perspective*. The most important step is to view the annual meeting from the context of your total, year-round communications, disclosure, and IR objectives. The annual meeting is not something to be run for its own sake or simply for compliance, separated from the rest of your investor communications.

• *Offer more ways to connect*. Virtual meeting technologies offer great opportunities for more effective communication and expanding your reach. Like many emerging IR communications applications, it's something you can add, rather than an either/or choice between physical or virtual meetings.

• *Increase transparency*. Make use of all disclosure channels to publicize the annual meeting before the event, and do the same following the meeting to quickly announce voting results.

• *Participate*. Directors ought to attend every annual meeting. Absence sends the absolute wrong message to your investors. Likewise, boards should use this as an opportunity for direct shareholder engagement (subject to common sense ground rules).

**Jeff Morgan** is president and CEO of the National Investor Relations Institute (www.niri.org). Founded in 1969, NIRI is the largest professional investor relations association in the world, with more than 3,500 members representing 2,000 publicly held companies. He can be contacted at jmorgan@niri.org.

## Overview & Background

Blue Harbour Group, L.P. ("Blue Harbour") is an investment firm, founded by Clifton S. Robbins in 2004. Blue Harbour's active ownership strategy employs a "private equity approach to the public markets." We seek to invest as a significant minority shareholder in fundamentally undervalued U.S. and Canadian companies with market capitalizations ranging from $500 million to $5 billion. As a significant minority shareholder, our objective is to work in collaboration with management to initiate strategic changes to unlock and create substantial shareholder value. Blue Harbour has established a reputation as a respected, value-added investor in numerous companies whose management teams serve as important references for new investment prospects. Since inception, the Blue Harbour funds have significantly outperformed relevant market indices.

## Investment Strategy

Blue Harbour pursues a value-oriented, active ownership investment strategy focusing on companies that have the opportunity to significantly enhance shareholder value through strategic corporate transactions, financial restructurings or initiatives arising from corporate governance or operational changes. As a trusted lead investor, Blue Harbour plays an active, collaborative role, working with the company to design and implement value enhancing initiatives. We are long term investors with a multi-year investment horizon.

## Private Equity Approach to the Public Markets

A critical component of our strategy is to support management teams who are committed to creating value for shareholders. We focus only on U.S. public companies that could create significant value by implementing strategic or financial change. Though we are minority investors, we approach screening, analysis and due diligence to identify fundamentally undervalued companies as if we intended to own the entire enterpri*se*. This means we look for undervalued companies with high quality businesses, attractive valuations, good industry dynamics, sustainable franchises and recurring free cash flow business models. By conducting proprietary research through a private equity lens, we are well-positioned to design and recommend initiatives that will unlock and create value, and often to assist the management in their implementation.

## Blue Harbour's Active Role

Blue Harbour seeks to enhance returns by proactively engaging managements and boards to create and unlock value in any of four areas: *Strategic Initiatives, Capital Structure, Corporate Governance, and Operations.*

## The Opportunity Set: Small to Mid-Cap Public Companies

There are approximately 2,000 U.S. and Canadian companies within the $500 million to $5 billion market capitalization range. We believe this universe will continue to provide a wealth of opportunities for our strategy. Wall Street research coverage for this sector has been significantly reduced, creating greater inefficiencies and opportunities. Furthermore, in recent years, boards and management teams generally have become more interested in considering ways to unlock value. Finally, high levels of cash on corporate balance sheets and committed and uninvested private equity funds represent significant sources of buyer interest in this space. This creates significant opportunities for Blue Harbour to design and introduce our value-enhancing ideas and strategies.

## The Blue Harbour Investment Team

Mr. Robbins is complemented by a team of senior professionals responsible for generating investment ideas, developing relationships with management teams, performing research and due diligence on prospective investments, and monitoring current portfolio investments. The team consists of professionals with an average of 10 years' experience in the areas of corporate finance, private and public market investing. The team's combined intellectual capital and experience have provided Blue Harbour with a distinguished reputation as a constructive long-term shareholder and committed partner.

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