

Activists Unite to Obtain Majority Support for Shareholder Proposal to Split a Company

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In an unusual collaboration, Relational Investors and CalSTRS succeeded this week in having a majority of shareholders support CalSTRS' shareholder proposal recommending that the board and management "act expeditiously" to engage an investment bank to effectuate a spinoff of Timken's steel business. CalSTRS' precatory resolution was favored by 53% of the votes cast. Given that insiders and affiliates own about 15% to 17% of the company, the activists claimed that at least 65% of non-affiliates supported the proposal.

Timken indicated that its board would evaluate the results and announce its next steps within 45 days. Relational and CalSTRS are threatening a proxy contest if the company does not follow through with the proposal's request. The two investors reportedly own 7% of the company together, although the company disclosed that CalSTRS' share ownership represents less than 1%.

While being far short of a proxy contest, the activist campaign was intense, as evidenced by the number of exempt solicitations filed by Relational and CalSTRS beginning in November, and additional soliciting materials submitted by the company in response. Each side also used social media, with dueling websites devoted to its version of the debate (Unlocktimken.com from the activists and TimkenDrivesValue.com by the company.)

ISS and Glass Lewis both supported the shareholder proposal. CalSTRS also took issue with the election of several director nominees, including the cousin of a founder serving as an independent director of the audit committee. In another example of how the activists' collaboration shifted the usual allegiances, a union of steelworkers strongly opposed the proposal.

Relational Investors argued that since the proposal is non-binding, a "yes" vote carries "no downside," but a "no" vote could send share price lower. Since the proposal was announced in November, the stock price has increased by 38%.

Shareholder proposals on major business strategies is uncommon. According to the *Wall Street Journal*, only 10 other such proposals to break up a company or divest assets have been made since 2005. Other companies also received proposals calling for board review of major transactions this year, but many were excluded on grounds of vagueness or under the ordinary business exception when the proposals combined both non-extraordinary and extraordinary transactions. The success of this one, however, could inspire other examples that withstand SEC challenge, and generate active campaigns.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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