

Shareholders Sues Darden on Advanced Notice Bylaw Changes

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Amid pressure to separate parts of its restaurant chain, Darden had decided to spin off Red Lobster. Two hedge funds, Barrington Capital and Starboard Value, previously proposed more drastic upheaval, such as splitting the restaurants into two groups representing mature businesses or faster growing lines. In December 2013, Starboard reported it held approximately 5.6% of the stock. Starboard is currently soliciting shareholder consents to call a special meeting to consider a non-binding proposal prior to the company's September annual meeting, that urges the Darden board not to approve any agreement or proposed transaction involving a Red Lobster separation or spinoff unless the transaction would require shareholder approval. The consent period ends this week and would require a majority of outstanding shares to vote in favor under Florida law. Starboard also indicated that it may nominate candidates to replace existing directors at the company's annual meeting.

In late March, the company amended its bylaws. The [Form 8-K](#) disclosed that the changes are intended to reflect "current market practice" by providing for the designation of Orange County, Florida, as the exclusive forum for certain types of shareholder litigation and to make several changes to its advance notice provisions related to proposing matters at shareholder meetings, including director nominations. These include requirements that shareholders continue to hold their shares through the date of the meeting and disclose information regarding their interests in the company, the business being proposed and their relationship with the shareholder nominees. Nominees also need to provide information with respect to independence and complete written questionnaires about their background and qualifications, as well as provide a written representation and agreement with respect to the nominee's entry into voting commitments and compensation or indemnification arrangements and compliance with corporate policies. The City of Birmingham Retirement and Relief System has sued Darden Restaurants over these bylaws.

Although the advance notice bylaw changes do not appear to deviate terribly from so-called "market practice," including, for example, asking for disclosure of a lengthy list of securities that may constitute derivative instruments, the complaint calls these advanced notice disclosure provisions "unintelligible and punitive." An investor was quoted in the *New York Post* as likening it to "a full body-cavity search" and the complaint argues that these disclosures may have no bearing on the matter being proposed by the shareholder. In addition, the complaint focuses on several amendments which allow the chairman to adjourn shareholder meetings by simply announcing it at the meeting, viewing this as an attempt to forestall a special meeting of shareholders. The chairman also has the ability to determine whether shareholder nominations comply with the bylaws or instead decide that the proposal is defective, again not an unusual provision. In addition, the plaintiff alleges that the prohibition on voting commitments and any undisclosed compensation, reimbursement or indemnification is unilaterally prohibitive in that they do not apply to existing directors. Finally, the bylaw modified the date of the annual meeting so that it need not be held only in September or October, an arguably innocent change in different circumstances.

Touching on a recent hot topic, the complaint notes that the terms of many Darden board members are "well beyond the average tenure" for public company boards, meaning "at least a decade," and questions those directors' ability to provide effective oversight. It alleges that "corporate democracy cannot resemble a dictatorship" if the rules surrounding the ability to nominate alternative directors are "rewritten to suit the will of the sitting directors." ISS and Glass Lewis both support Starboard's consent solicitation for a special meeting. The cancellation of a major investor conference caused ISS to write in its report that the challenge to the board "may never reach a moment of denouement." Both proxy advisory firms also questioned whether the bylaw changes "go beyond modernization" and in particular, noted that the timing puts the boards' motive in doubt. Indeed, given the nature of the changes, timing may be everything in this situation.

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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