SHAREHOLDER-DRIVEN CORPORATE GOVERNANCE AND ITS NECESSARY LIMITATIONS: AN ANALYSIS OF WOLF PACKS

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CONTENTS

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INTRODUCTION

Today's capital market composition differs significantly from the Berle and Means' view that the modern corporation is one characterized by the separation of ownership and control.[1] Institutional investors, such as pension funds and hedge funds, are active in governance, often seeking changes over and above those that yield a mere return on their investment. To some extent, public corporations with shareholders who demand greater accountability and more input have been willing to accede to shareholder wishes. This relationship between corporation and shareholder has shifted largely because of the increased size, sophistication, and prevalence of institutional investors in the capital markets.

This Article focuses on the rise and behavior of institutional investors. Their influence as shareholders is undeniable, and is even more palpable when they band together in groups called "wolf packs."[2] A wolf pack is a loose network of parallel-minded shareholders (typically hedge funds) that act together to effect change in a given corporation without necessarily disclosing their collective interest.[3] Wolf packs are able to circumvent securities laws by deliberately avoiding being characterized as a "group" or as "acting jointly or in concert."[4] As is the case with a group of prowling wolves, the lead wolf (shareholder) might be visible to its prey while the other wolves (shareholders) appear only when necessary.

This Article probes the role of wolf packs in developed market economies and particularly in change of control transactions, including proxy contests. Changes of control, especially when hostile, are controversial given that the target may

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[1] *See* ADOLF A. BERLE & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (MacMillan rev. ed. 1967).

[2] There is a significant amount of debate on this topic in U.S. literature. For literature advocating for greater shareholder empowerment, see, for example, Lucian Bebchuk, *Letting Shareholders Set the Rules*, 119 HARV. L. REV. 1784 (2006); and Lucian Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833 (2005) [hereinafter Bebchuck, *Increasing Shareholder Power*]. For literature advocating for corporate laws that place greater power in the board of directors, see, for example, Iman Anabtawi, *Some Skepticism About Increasing Shareholder Power*, 53 UCLA L. REV. 561 (2006) and Stephen M. Bainbridge, *Director Primacy and Shareholder Disempowerment*, 119 HARV. L. REV. 1735 (2006).

[3] John C. Coffee, Jr. & Darius Palia, *The Wolf at the Door: The Impact of Hedge Fund Activism on Corporate Governance*, 41 J. CORP. L. 545, 562 (2016) (describing "wolf pack" terminology).

[4] Under U.S. securities law, shareholders acting as a "group" must disclose their collective interest. *See* 15 U.S.C. § 78m(d)(1), (3) (2012). Under Canadian securities law, shareholders acting "jointly or in concert" are subject to disclosure rules. *See* National Instrument 62-104, *Take-over Bids and Issuer Bids* § 1.9 (May 5, 2016), http://www.osc.gov.on.ca/documents/en/Securities-Category6/ni_20160505_62-104_take-over-bids.pdf [https://perma.cc/CM6X-WKS7]. For the Securities and Exchange Commission's ("SEC") view on this, see Liz Hoffman, Aruna Viswanatha & David Benoit, *SEC Probes Activist Funds Over Whether They Secretly Acted in Concert*, WALL STREET J. (June 4, 2015, 4:54 PM), https://www.wsj.com/articles/sec-probes-activist-funds-over-whether-they-secretly-acted-in-concert-1433451205.

have other strategic intentions that the board conceives to be in its long-term best interests.[5] Wolf packs add another dimension to changes of control, as they typically form before share price appreciation, which occurs in a change of control transaction.[6] Further, they are able to overcome the coordination costs and other impediments that smaller shareholders experience in forming *de facto* blocks, thereby making the threat of a proxy contest or a push for a sale of the company more viable.[7]

This Article furthers the analysis of wolf pack formation by isolating conditions (i.e. in addition to timing) that might engender shareholder coordination. In particular, there are certain circumstances in which shareholder cooperation generally, and wolf pack behavior specifically, are able effectively to overcome coordination costs. First, corporations characterized by large institutional shareholders facilitate wolf pack formation because these shareholders are generally sophisticated rational actors that can coordinate with each other relatively easily. Second, as sophisticated actors, these shareholders may be motivated by the usual share price increase that tends to follow the filing of mandated disclosures when shareholders pass prescribed thresholds of ownership in a corporation's shares. Third, coordination among wolf pack members is facilitated by corporate and securities laws, which explicitly allow coordination among a small group of shareholders and can drive the lead activist to focus its recruitment efforts on larger shareholders. This argument is especially pertinent to capital markets that are characterized by institutional shareholders that hold sizable positions in public corporations.[8]

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[5] *See infra* Part I.

[6] *See infra* Part II.

[7] *See infra* Part II.

[8] *See* Richard Bozec, Mohamed Dia & Yves Bozec, *Corporate Ownership and Governance Practices in Canada: A Longitudinal Study*, 4 INT'L J. CORP. GOVERNANCE 51, 59 (2013) (finding that fifty-eight percent of Canadian issuers feature at least one controlling shareholder that owns shares representing more than ten percent of the voting rights in respect the issuer); *see also* Randall K. Morck, David A. Stangeland & Bernard Yeung, *Inherited Wealth, Corporate Control, and Economic Growth: The Canadian Disease?*, *in* CONCENTRATED CORPORATE OWNERSHIP 319, 319 (Randall K. Morck ed., 2000) (finding that "countries in which billionaire heir's wealth is large relative to GDP grow more slowly than other countries at similar levels of development while countries in which self-made entrepreneur billionaire wealth is large relative to GDP grow more rapidly"). The United States is generally thought to have a more dispersed ownership structure. However, a study by Professor Clifford Holderness finds that ninety-six percent of U.S. firms have a blockholder holding at least five percent of the firm's common stock, with the average holding being thirty-nine percent. Clifford G. Holderness, *The Myth of Diffuse Ownership in the United States*, 22 REV. FIN. STUD. 1377, 1382 (2009). In contrast, ownership in the United Kingdom is more dispersed, with ninety percent of companies listed on the London Stock Exchange ("LSE") having no major shareholder owning twenty-five percent or more. ORGANIZATION FOR ECONOMIC CORPORATION AND DEVELOPMENT, OECD CORPORATE GOVERNANCE FACTBOOK 2017, at 14 (2017). Finally, ownership concentration in the E.U. is quite varied. For example, in Italy nearly two-thirds of companies are controlled by a single

Thus, the focus here is on investor sophistication as a contributing element to wolf pack formation. This Article also highlights the benefits of wolf packs for smaller, less sophisticated shareholders who free-ride on the activism of the lead wolf or shareholder. Finally, it analogizes wolf packs to blockholders in terms of the monitoring function that the lead wolf and blockholder play. This Article does not argue that wolf packs should ride above the law; disclosure of their joint conduct is important in ensuring that wolf packs underpin informationally efficient capital markets.

The entire discussion that follows occurs against the backdrop of a new concept of governance called "Shareholder-driven Corporate Governance" ("SCG"), an alternative to the contractarian model of governance.[9] SCG is a descriptive term with practical import, explaining the ongoing phenomenon of shareholder activism and the corresponding shift in the balance of power within public corporations.[10] It is also a normative concept in the sense that it presents a goal to which lawmakers (not to mention investors) may aspire, especially in light of concerns relating to management and board entrenchment.[11]

In jurisdictions throughout the world, reform agendas and board decision-making evidence a movement toward SCG and away from Berle and Means' understanding of shareholders as mere passive agents in the corporation.[12] The Dodd-Frank say-on-pay reforms are a prime example, as is proxy voting and the increasingly popular move to separate the roles of board chair and CEO.[13] The rise of institutional shareholders and wolf pack formation are also an example and, of course, the subject of this Article.

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shareholder while in the Netherlands the largest shareholder in sixty-two percent of companies held less than ten percent. *Id.* at 13.

[9] *See* ANITA INDIRA ANAND, SHAREHOLDER-DRIVEN CORPORATE GOVERNANCE (forthcoming 2019) (manuscript at 6), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3249665.

[10] *See id.* (manuscript at 7).

[11] *See, e.g.*, Anita Anand, *Implications of Shareholder Activism*, *in* GLOBAL CAPITAL MARKETS 17, 27-29 (P.M. Vasudev & Susan Watson eds., 2017) (discussing management and board entrenchment). For an SCG-oriented analysis of wolf pack activism, see generally Anita Anand & Andrew Mihalik, *Coordination and Monitoring in Changes of Control: The Controversial Role of "Wolf Packs" in Capital Markets*, 54 OSGOODE HALL L.J. 377 (2017).

[12] *See* BERLE & MEANS, *supra* note 1; Bebchuk, *Increasing Shareholder Power*, *supra* note 2, at 842; Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 113 COLUM. L. REV. 863, 865 (2013) (explaining that "Berle-Means premise of dispersed share ownership is now wrong"); Lynn A. Stout, *On the Rise of Shareholder Primacy, Signs of its Fall, and the Return of Managerialism (in the Closet)*, 36 SEATTLE U. L. REV. 1169, 1178 (2013) ("Shareholders now have more influence over boards, and executives now are more focused on share price, than at any time in business history.").

[13] In Canada, the 2016 amendments to takeover bid law, introducing a fifty percent minimum tender requirement before a bid can be successful, advance the aims of SCG. *See* Anita Anand, *The Future of Poison Pills in Canada: Are Takeover Bid Reforms Needed?*, 61 MCGILL L.J. 1, 4 (2015).

Part I sets forth the concept of "shareholder-driven corporate governance," and responds to its critics, as a means to lay the theoretical background for the discussion of wolf packs to follow. Part II analogizes wolf packs to blockholders generally and examines characteristics of capital markets that facilitate wolf pack formation. Part III considers and evaluates the legal regime applicable to wolf packs, and argues that, for the purposes of disclosure rules, wolf packs should be treated in the same manner as blockholders because the two perform similar roles in the corporation.

I. SHAREHOLDER-DRIVEN CORPORATE GOVERNANCE

While corporate law scholarship exploded in the post-Enron period,[14] our collective thinking about corporate theory did not develop at a similar pace. The academic literature generally falls into one of three categories: the shareholder versus director primacy debate,[15] stakeholder theory including corporate social responsibility,[16] and law and economics scholarship (or a critique of it).[17] As a whole, this literature takes as its starting point the Berle and Means model of the corporation, which is built on the idea that those who own the corporation (the shareholders) are passive, disinterested, or uninvolved in the control of the corporation.

This Article differs from the bulk of academic writing on corporate governance in that it does not adhere to the Berle and Means model of the corporation. What does increased shareholder activism generally, and wolf pack behavior specifically, mean for theoretical conceptions of the corporation?

An implication of the Berle and Means model is that directors and managers, as rational actors, may seek to entrench themselves, and they may shirk their duties or divert corporate resources for their own benefit at the expense of shareholders.[18] They may make themselves so valuable to the corporation that

[14] For literature on the Sarbanes-Oxley Act, see, for example, William W. Bratton, *Enron, Sarbanes-Oxley and Accounting: Rules Versus Principles Versus Rents*, 48 VILL. L. REV. 1023 (2003); Kathleen F. Brickey, *From Enron to Worldcom and Beyond: Life and Crime After Sarbanes-Oxley*, 81 WASH. U. L.Q. 357 (2003); Larry E. Ribstein, *Market vs. Regulatory Responses to Corporate Fraud: A Critique of the Sarbanes-Oxley Act of 2002*, 28 J. CORP. L. 1 (2002); Kelly E. Carter, Capital Structure Behavior of Domestic and Cross-Listed Firms: Evidence from the Sarbanes-Oxley Act of 2002 (Jan. 2, 2011) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1664204; Teodora Paligorova, The Effect of the Sarbanes-Oxley Act on CEO Pay for Luck (Oct. 27, 2008) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1101094; and .

[15] *See, e.g.*, STEPHEN M. BAINBRIDGE, CORPORATE GOVERNANCE AFTER THE FINANCIAL CRISIS 10-12 (2012).

[16] *See, e.g.*, Edward Freeman & John McVea, *A Stakeholder Approach to Strategic Management*, *in* THE BLACKWELL HANDBOOK OF STRATEGIC MANAGEMENT (Michael A. Hitt, Edward R. Freeman & Jeffery S. Harrison eds., 2001) .

[17] *See, e.g.*, Lawrence E. Mitchell, *Groundwork of the Metaphysics of Corporate Law*, 50 WASH. & LEE L. REV. 1477, 1479-81 (1993).

[18] Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 308 (1976) (explaining that

they are too costly to replace.[19] They may also forego investments in profitable ventures by investing in specialized projects that require their unique expertise, even if these specialized alternatives will not be as profitable.[20] Some argue, contrary to empirical evidence,[21] that managers do not entrench themselves.[22] However, as long as it is *possible* for management to prioritize its own interests above those of the corporation, the concept of management entrenchment remains relevant.[23]

Writing initially in the 1930s, Berle and Means did not consider the role of the institutional shareholder in corporate governance.[24] While they viewed shareholders to be generally passive, they did not mean to say that shareholders were irrational.[25] They reasoned that it was cost-effective for shareholders to be inactive in their relationship with the corporation.[26] In order to make an informed vote, shareholders would have to engage in time-consuming research, find and consider appropriate advice, consult with others, and weigh the alternatives. The costs of engagement simply outweighed its benefits, the result being that managers dominated the corporation and its assets with little shareholder resistance.

Berle and Means's work dominated the corporate law literature for decades.[27] However, in the years since they wrote, the shareholder composition of the

sometimes there will be "divergence between the agent's decisions and those decisions which would maximize the welfare of the principal"); *see also* FRANK EASTERBROOK & DANIEL FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 122 (1991).

[19] Andrei Shleifer & Robert W. Vishny, *Management Entrenchment: The Case of Manager-Specific Investments*, 25 J. FIN. ECON. 123, 125 (1989) ("[E]xcessive growth of the firm in the directions suggested by the CEO's talents and experience is a means of entrenchment.").

[20] *Id.* ("Corporate managers invest in businesses related to their own background and experience, even when such investments are not profitable for the firm.").

[21] Lucian A. Bebchuk & Ehud Kamar, *Bundling and Entrenchment*, 123 HARV. L. REV. 1549, 1554 (2010) (concluding that empirical data calls for reconsidering fundamental corporate law principles); Paul Borochin & John D. Knopf, Do Managers Seek Control and Entrenchment? 23 (Nov. 6, 2018) (unpublished manuscript), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2670918 ("Our evidence suggests that managers implement a multifaceted plan to become entrenched.").

[22] *See, e.g.*, ALFRED D. CHANDLER, THE VISIBLE HAND: THE MANAGERIAL REVOLUTION IN AMERICAN BUSINESS 54 (1977). On the role of the board in keeping managers from entrenching themselves, see Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW. U. L. REV. 547, 599-605 (2003).

[23] *See* Anand, *supra* note 13, at 15.

[24] *See* BERLE & MEANS, *supra* note 1, at 1.

[25] *See id.*

[26] WOLF-GEORG RINGE, THE DECONSTRUCTION OF EQUITY: ACTIVIST SHAREHOLDERS, DECOUPLED RISK, AND CORPORATE GOVERNANCE 7-10 (2016).

[27] The Berle and Means paradigm was not without controversy. In particular, some scholars argued that shareholders are not the "owners" of the corporation *per se*, but rather that they hold contractual rights as a result of the share purchase without owning the corporation outright. *See, e.g.*, LYNN STOUT, THE SHAREHOLDER VALUE MYTH 2 (2012). We

capital markets has undergone massive transformation. In the 1950s, individual investors held about ninety percent of the U.S. equity markets, while institutional investors held only six percent.[28] Today, institutional investors hold around sixty-six percent of the equity market.[29] Many of today's shareholders cannot be classified as rationally apathetic retail shareholders; rather, they are sophisticated, often seeking governance changes in addition to a return on their investment. Some are hedge funds that look for undervalued companies to purchase and turn around.[30] Others are institutional investors, such as pension funds, that seek long-term investments on behalf of beneficiaries to whom they owe a fiduciary duty.

We can characterize this new capital market environment as one that evidences SCG. SCG identifies and defines a corporate governance approach that seeks to protect shareholders' interests while also affirming their involvement in governance. It captures both actual and potential governance strategies. SCG is a descriptive term with practical import, explaining the ongoing phenomenon of shareholder activism and the corresponding shift in the balance of power within public corporations. It is also a normative concept in the sense that it presents a goal to which lawmakers (not to mention investors) may aspire, especially in light of on-going concerns relating to management and board entrenchment. Proxy voting, say-on-pay, and the increasingly popular move to separate the roles of board chair and CEO are prime examples of SCG.

In an environment characterized by sophisticated shareholders and SCG, the concept of monitoring endures. Indeed, the incentives for institutional investors

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will return to this argument shortly. Professor Stephen Bainbridge offers an argument rejecting the idea of shareholder ownership from a different perspective:

> In contrast, contractarians reject the idea that the firm is a thing capable of being owned. Recall that the firm is, or has, a nexus for the set of contracts by which various factors of production are hired. Someone owns each of those factors, but no one owns the nexus itself. To be sure, most theories of the firm agree, shareholders own the residual claim on the corporation's assets and earnings. The ownership of that claim explains why the set of contracts comprising the corporation treats the shareholders as the beneficiaries of director accountability. Yet, ownership of the residual claim is not the same as ownership of the firm itself.

See Bainbridge, *supra* note 22, at 564-65.

[28] LISA M. FAIRFAX, SHAREHOLDER DEMOCRACY: A PRIMER ON SHAREHOLDER ACTIVISM AND PARTICIPATION 45-46 (2011).

[29] *Id.* at 45-46 (indicating that in 2009 institutional investors held around fifty or sixty-six percent of equity market).

[30] *See* Marcel Kahan & Edward B. Rock, *Hedge Funds in Corporate Governance and Corporate Control*, *in* INSTITUTIONAL INVESTOR ACTIVISM: HEDGE FUNDS AND PRIVATE EQUITY, ECONOMICS AND REGULATION 145, 151-52 (William W. Bratton & Joseph A. McCahery eds., 2015) (analyzing implications of rising hedge funds for corporate governance and corporate control); *see also* John Armour & Brian Cheffins, *The Rise and Fall (?) of Shareholder Activism by Hedge Funds*, *in* INSTITUTIONAL INVESTOR ACTIVISM: HEDGE FUNDS AND PRIVATE EQUITY, ECONOMICS AND REGULATION, *supra*, at 198, 206 (discussing rise of phenomenon in 2000s of shareholder activism associated with hedge funds).

to monitor (including their willingness to internalize the costs of free-riding) vary with the size of their shareholdings.[31] "[S]mall investors can only absorb a negligible share of the firm's risk, leaving them without sufficient incentives to monitor."[32] Put another way, only large shareholders will (or can afford to) monitor firms.[33] Evidence further suggests that multiple small blockholders are not as effective in influencing corporate decision-making as is a single large blockholder, partly because coordination costs among small blockholders impede their ability to monitor the firm.[34] As such, a group of small shareholders that collectively owns a block of shares equivalent in size and right to a block owned by a single, large blockholder will likely result in less effective monitoring.[35] It is simply more difficult to organize behavior amongst dispersed shareholders, even if they are in a group,[36] especially when shareholders have heterogeneous preferences.[37]

SCG sets forth an undoubtedly controversial claim, but is supported by empirical research. For example, Professors Lucian Bebchuk, Alon Brav, and Wei Jiang find that short-term gains from shareholder activism, particularly on the part of hedge funds, do not come at the expense of long-term performance.[38]

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[31] Andrew Winton, *Limitation of Liability and the Ownership Structure of the Firm*, 48 J. FIN. 487, 493 (1993) (discussing how large investors will monitor managers more than small investors).

[32] *Id.*

[33] Amrita Dhillon & Silvia Rossetto, *Corporate Control and Multiple Large Shareholders* 31-32 (Univ. of Warwick, Working Paper No. 891, 2009), https://www2.warwick.ac.uk/fac/soc/economics/staff/academic/dhillon/wp/submission16nov09.pdf [https://perma.cc/ZQ3H-5ALF] (explaining that high costs are associated with monitoring).

[34] *See* Winton, *supra* note 31, at 497-98.

[35] John Armour, Henry Hansmann & Reinier Kraakman, *Agency Problems and Legal Strategies*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 29, 29 (2017) ("[T]he value of the agent's performance to the principal will be reduced, either directly or because, to assure the quality of the agent's performance, the principal must engage in costly monitoring of the agent."). Although the presence of a single, large blockholder tends to increase shareholder monitoring of management, it is worth bearing in mind the possibility that the blockholder will seek to extract private benefits of control to the detriment of other shareholders (as discussed more fully below).

[36] *See, e.g.*, Andrew M. Kulpa & Butzel Long, *The Wolf in Shareholder's Clothing: Hedge Fund Use of Cooperative Game Theory and Voting Structures to Exploit Corporate Control and Governance*, 6 U.C. DAVIS BUS. L.J. 4, 4 (2005).

[37] Armour, Hansmann & Kraakman, *supra* note 35, at 30. It is worth noting, however, that the coordination issues that hinder shareholder intervention strategies actually make the threat of exit stronger, thereby allowing many small blockholders to have a positive impact on managerial discipline. *See* Alex Edmans & Gustavo Manso, *Governance Through Trading and Intervention: A Theory of Multiple Blockholders*, 24 REV. FIN. STUD. 2395, 2396 (2011) (arguing that threat of trading activity of multiple blockholders in the face of poor managerial performance disciplines management). Even so, wolf packs ostensibly form to intervene and agitate for change, not to passively invest and then exit.

[38] Lucian A. Bebchuk, Alon Brav & Wei Jiang, *The Long-Term Effects of Hedge Funds Activism*, 115 COLUM. L. REV. 1085, 1087, 1089 (2015) (concluding that view that activists

Their research undermines the view that activist interventions are costly to firms and their shareholders in the long term.[39] Thus, we should not dismiss activist behavior as serving the activist alone.

SCG will be viewed skeptically by some. While Professor Stephen Bainbridge acknowledges that imperial CEOs are undesirable,[40] he views the historic separation of shareholders' ownership and board control not as a problem to be solved, but as a unique invention that has allowed modern corporations to flourish. Accordingly, he argues that efforts to give shareholders more power should be resisted, as shareholders suffer from inferior information and divergent interests, making them poor decision-makers (at least in terms of the entire organization).[41] Every large organization needs a model that facilitates effective decision-making. Placing the ultimate decision-making authority in the board of directors, Bainbridge argues, strikes the appropriate balance between authority and accountability.[42] Consequently, shareholder voting only exists as an "accountability mechanism" of last resort, such as in the event that managers and directors have performed well below expectations and are therefore subject to a takeover fight worth waging.[43]

While shareholders may make poor managers given their lack of information and divergent interests, shareholder participation in governance should not be conceived of as a tool of last resort. The sophistication of institutional shareholders and activists is a defining difference between the shareholders of whom Berle and Means (and Bainbridge) speak and the shareholders of today. In light of this sophistication, and the meaningful input that shareholders can provide, it makes sense to allow shareholders greater scope for participation in the affairs of the corporation. Of course, corporate law already allows

with short investment horizons have incentive to increase short-term prices is not empirically supported); *see also* Andrew Carrothers, *Friends or Foes? Activist Hedge Funds and Other Institutional Investors*, 3 ECON. & BUS. REV. 38, 39 (2017) (explaining that "hedge funds do not avoid targets with high levels of institutional ownernship and that the trading behavior of institutional investors with different investment time horizons is consistent with hedge fund activism creating value") .

[39] *See, e.g.*, Bebchuk, Brav & Jiang, *supra* note 38, at 1141-47. Additionally, Professors K.J. Martijin Cremers and Simone Sepe, who find that whether institutional ownership has a positive or negative effect on firm value depends on a variety of factors, including the specific firm characteristics, level of institutional ownership, and the institutional investor's propensity towards activism. K.J. Martijn Cremers & Simone M. Sepe, *Institutional Investors, Corporate Governance, and Firm Value*, 41 SEATTLE U. L. REV. 387, 388-89 (2018).

[40] BAINBRIDGE, *supra* note 15, at 82-88 (reviewing historical trend toward and implication of board independence).

[41] *Id.* at 88 ("Hence, insofar as efficient decision making is the goal of corporate governance, independence may not be desirable.").

[42] *Id.* at 27 ("Yet, it turns out that corporate law also was wise to assign ultimate decision-making authority to a group . . . rather than a single individual.").

[43] *Id.* at 101-04 ("For example, managers of a firm with strong takeover defenses are less subject to the constraining influence of the market for corporate control than are those of a firm with no takeover defenses.").

shareholders to communicate with each other and, if they disagree with the decisions of the board, to participate in governance via the dissident proxy process. It also allows them to file shareholder proposals and to requisition shareholder meetings. These rights are part of a broader statutory framework which, along with securities regulation, is designed to protect investors generally and circumscribe the power of the board.[44]

Shareholders, especially institutional shareholders, are increasingly sophisticated as corporate monitors. It therefore stands to reason that they would seek greater participation in a corporation's governance, including meaningful access to the nomination processes for electing directors (so-called "proxy access") and majority voting.[45] Thus, as SCG contemplates, we have entered a new phase of corporate governance where shareholders, particularly hedge funds and other institutional shareholders, are more emboldened and more influential in corporate governance.

Because of their sophistication, institutional investors arguably allay concerns that Professors Zohar Goshen and Richard Squire introduce in their principal cost theory.[46] They argue that investors should not only be concerned with increased agency conflict costs (arising from conflicting interests between managers and investors), but also with three other types of costs: principal competence costs (arising from investor mistakes due to a lack of expertise); agent competence costs (arising from honest mistakes by management); and principal conflict costs (arising from conflicting interests among investors).[47] These different costs arise on a spectrum of intensity depending on how

[44] These rights vary considerably from one jurisdiction to the next. In the Canadian context, see Canada Business Corporations Act, R.S.C. 1985, c C-44, s 137, 143, 239. In the American context, see 17 C.F.R. § 240.14a-8 (2018) for shareholder proposals. Unlike Canada, there is no shareholder right to requisition a meeting under Delaware or U.S. federal law. U.K. law does more to facilitate shareholder control, giving shareholders with five percent or more of a corporation a right to have their proposals included in proxy materials and to requisition meetings. *See* Companies Act 2006, c. 46, § 292 (U.K.). U.K law does not give boards discretionary power to set aside binding proposals. *See id.*

[45] In Canada, a recent bill amended the Canada Business Corporations Act with some provisions that enhanced shareholder democracy. *See* Bill C-25, *An Act to Amend the Canada Business Corporations Act, the Canada Cooperatives Act, the Canada Not-for-Profit Corporations Act and the Competition Act*, 1st Sess, 42d Parl, 2018. Given Royal Assent on May 1, 2018, Bill C-25 requires that directors receive a majority vote and allows shareholders to vote against a nominee's election rather than simply withholding a vote. *See id.* A director who receives less than a majority of votes will be removed from the board within ninety days. *See id.* The Bill also replaces slate voting with individual elections for individual nominees. *See id.*; *see, e.g.*, Lucian A. Bebchuk, *The Myth of Shareholder Franchise*, *in* INSTITUTIONAL INVESTOR ACTIVISM: HEDGE FUNDS AND PRIVATE EQUITY, ECONOMICS AND REGULATION, *supra* note 30, at 1, 72.

[46] *See* Zohar Goshen & Richard Squire, *Principal Costs: A New Theory for Corporate Law and Governance*, 117 COLUM. L. REV. 767, 790-95 (2017).

[47] *Id.* at 791-95.

ownership and control exist in a particular firm.[48] Goshen and Squire emphasize that shareholders are not experienced managers bound by a fiduciary duty to the corporation.[49] They argue that the optimal arrangement of control in a particular firm is contextual (i.e. firm-specific).[50] They contend that this insight explains why empirical studies find no consistent relationship between blockholding and overall financial performance: in some firms, blockholdings will be value-decreasing, while in others they will be value-increasing.[51]

Principal cost theory presents a powerful argument but does not undermine the thesis that as sophisticated actors, institutional shareholders, especially those who act in concert, can be effective monitors and enhance firm accountability. They do not lack expertise and, given that they are acting together, do not (generally speaking) fall prey to the hypothesis of Goshen and Squire.[52]

Despite the potential costs arising from increased shareholder participation in management, it is at least arguable that the presence of institutional shareholders can have a beneficial effect on the firm's governance in reducing agency costs through monitoring. Indeed, the empirical work of Bebchuk, Brav, and Jiang provides persuasive evidence of the positive long-term effects of hedge fund acvitism.[53] As discussed in Part II, under certain conditions, wolf packs comprised of large institutional shareholders are able to overcome the coordination costs that impede blocks comprised of smaller shareholders. In this way, they can be even more effective than a single, large blockholder.

II. WOLF PACK BEHAVIOR

As discussed above, a new era of corporate governance—one characterized by SCG and its focus on the rise of institutional investors—has emerged. Recognizing that corporate law seeks to mediate between a corporation's directors and its shareholders by assigning each a distinct set of legal rights,[54]

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[48] *Id.* at 797.

[49] *Id.* at 798-99.

[50] *Id.* at 796.

[51] *Id.* at 805-07, 815 ("The use of a dual-class share structure is a good illustration of the firm-specific nature of corporate governance, as the structure may be well-suited to firms in complex industries such as information technology (e.g., Google, Facebook, and LinkedIn), or to firms whose outside shareholders recognize management's unique skills and strategic vision (e.g., Berkshire Hathaway). It is nonetheless an extreme option on the governance-structure menu, and it is uncommon among public firms in the United States.").

[52] *See supra* note 39 and accompanying text.

[53] *See, e.g.*, Bebchuk, Brav & Jiang, *supra* note 38, at 1140, 1146, 1148. *But see* Alessio M. Pacces, *Exit, Voice and Loyalty from the Perspective of Hedge Funds Activism in Corporate Governance*, 9 ERASMUS L. REV. 199, 206-07 (2016) (reviewing and critiquing commonly used empirical methodology).

[54] According to Robert Dickerson's report, balancing the tension between directors and shareholders is the normative underpinning of Canadian corporate law. ROBERT W. V. DICKERSON, JOHN L. HOWARD & LEON GETZ, PROPOSALS FOR A NEW BUSINESS CORPORATIONS LAW FOR CANADA 3 (1971) ("Nor can we see any practical way that, at least in the 'public'

this Part considers issues that can arise when shareholders are accorded too much power over how a company is run.

SCG asserts the need to reconsider the historical division between ownership and control in publicly-traded corporations.[55] It acknowledges that benefits accrue to investors, and the corporation as a whole, as a result of shareholder activism.[56] For example, the size and sophistication of large institutional investors enable them to monitor management and even play an active role in steering the corporation. Smaller shareholders, who individually lack the means to operate as activists, benefit from having larger players protect interests parallel to their own.[57] But while shareholder activism has many economic benefits, it also creates new challenges.

The emergence of "wolf packs" is an important case in point. Wolf packs are loose networks of like-minded shareholders (typically hedge funds) that act together to effect change in a corporation without disclosing their collective interest.[58] Wolf packs commonly feature alliances between a hedge fund, as a lead activist, and one or more fellow institutional investors.[59] Just as institutions that own large blocks of a company may hold sufficient sway to have a significant impact on the firm's value, a group of individually smaller blockholders operating in tandem under the direction of a pack leader can have

corporation, shareholders could be involved in corporate administration. This is not to say, however, that directors should not be responsible for their actions and accountable to shareholders and others for what they do.").

55 *See, e.g.*, BERLE & MEANS, *supra* note 1.

56 *See, e.g.*, *id.*

57 *See* Gaia Balp, *The Corporate Governance Role of Retail Investors*, OXFORD BUS. L. BLOG (July 23, 2018), https://www.law.ox.ac.uk/business-law-blog/blog/2018/07/corporate-governance-role-retail-investors [https://perma.cc/B54D-3Q67] (asserting that smaller shareholders may also play important corporate governance role in monitoring controlling shareholders).

58 John C. Coffee, Jr., *Hedge Fund Activism: What Do We Know and Not Know?*, *in* INSTITUTIONAL INVESTOR ACTIVISM: HEDGE FUNDS AND PRIVATE EQUITY, ECONOMICS AND REGULATION, *supra* note 30, at 690, 701-05; Coffee, Jr. & Palia, *supra* note 3, at 562; *also* Anand & Mihalik, *supra* note 11, at 385 (arguing that wolf packs perform an important monitoring function).

59 For example, a successful hedge fund led wolf pack campaign involved the 2014 sale of PetSmart to BC Partners. *See* Karlee Weineman, *BC Partners Offers $8.7B for PetSmart in 2014's Biggest LBO*, LAW360 (Dec. 14, 2014, 7:12 PM), https://www.law360.com/articles/604572/bc-partners-offers-8-7b-for-petsmart-in-2014-s-biggest-lbo. The wolf pack led by Jana Partners and supported by Longview Asset Management, amassed a twenty percent stake in the struggling company and forced the board to sell. *Id.* An additional example is the 2013 fight between Third Point Capital Management and the auction company Sotheby's. Andrew Brooks, *Shareholder Activism: Together Is Better*, SMITH SCH. BUS.: BUS. INSIGHT (Nov. 11, 2016), https://smith.queensu.ca/insight/articles/shareholder_activism_together_is_better [https://perma.cc/5VRT-BDWN]. Third Point, in tandem with Marcato Capital Management, successfully sought control over Sotheby's through the nomination of three new directors, including Third Point CEO Dan Loeb. *Id.*

a similar impact.[60] In other words, wolf packs, as a type of blockholder, can perform an important monitoring function.

Reliable empirical data on the incidence of wolf packs are challenging to obtain, since ungrouped shareholders bear no legal obligation to make disclosures in connection with their collective position.[61] As argued below, however, wolf packs comprised of institutional investors will form when the benefits of coordination exceed the costs of coordination. Indeed, two hypotheses explaining wolf pack formation dominate the nascent academic literature.[62] Under what we can term the "explicit coordination model," Professors John Coffee and Darius Palia argue that a lead activist will recruit other investors to join the pack *before* filing the required disclosure (a Schedule 13D).[63] Subsequent members of the pack are rewarded with a riskless arbitrage opportunity in return for their support of the lead activist's agenda: the lead activist tips off the pack's other members before filing its Schedule 13D, which is generally associated with a jump in the share price.[64] As such, the wolf pack is formed before disclosure is made through the explicit coordination efforts of the lead activist. As Professor William Bratton notes, although the purchase activity of subsequent members of the pack makes it more expensive for the lead activist to make further purchases in the target corporation, that the lead activist is required to share its gains with other members of the pack does not inhibit the activist from assuming a lead position.[65]

Under an alternative hypothesis, which we call the "implicit coordination model," Brav and others assert that a coordination game drives wolf pack formation, since individual shareholders are incentivized to join wolf packs without explicit coordination by a lead member.[66] A wolf pack can arise

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[60] *See* Anand & Mihalik, *supra* note 11, at 383 (noting empircal evidence suggesting relationship exists between blockholders and firm value).

[61] *See* Marco Becht et al., *Returns to Hedge Fund Activism: An International Study*, 30 REV. FIN. STUD. 2933, 2942 (2017) (explaining difficulty with measuring number of groupings among hedge fund activists).

[62] This Part draws from Anand & Mihalik, *supra* note 8, at 377-96. *See also* Yu Ting Forester Wong, Wolves at the Door: A Closer Look at Hedge Fund Activism 2 (Sept. 8, 2010) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2721413 (investigating two hypotheses, including coordinated effort hypothesis and spontaneous formation hypothesis).

[63] Coffee, Jr. & Palia, *supra* note 3, at 562-63, 565-66.

[64] *See* Anand & Mihalik, *supra* note 11, at 385; Coffee, Jr., & Palia, *supra* note 3, at 565-66.

[65] William W. Bratton, *Hedge Funds and Governance Targets: Long-Term Results* 4-6 (Univ. Pa. Inst. for L. & Econ., Research Paper No. 10-17, 2010), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1677517. Importantly, just as members of the wolf pack are careful to avoid acting in groups for the purposes of disclosure rules, they are also careful not to breach insider trading and tipping laws.

[66] *See generally* Alon Brav, Amil Dasgupta & Richmond Mathews, *Wolf Pack Activism* (European Corp. Governance Inst., Working Paper No. 501, 2018). In fact, in roughly half of wolf packs, there is no "leader" who holds the largest ownership stake. *See* Dionysia

spontaneously because investors monitor the same corporations at substantially the same times. Each small independent investor on its own lacks sufficient incentive to monitor and intervene because the probability of a successful campaign is low and the expected benefits do not outweigh the costs. However, the entry of a single, large investor, who is revealed to smaller investors through filing disclosure when it amasses more than five percent ownership, operates as a catalytic event that increases the expected probability of a successful intervention, which in turn compels small investors to join the intervention and form a wolf pack. The rational self-interest of the wolf pack members is sufficient for the wolf pack to form on the basis of implicit coordination *after* the lead activist discloses its position to the market.[67]

Quite apart from these two coordination models, an alternative way to understand wolf packs is to agree that a number of unique conditions are necessary to give rise to coordination among the wolf pack's members. The first condition, or non-condition, relates to the nature of the target corporation's shareholder base. If a corporation is widely held, the formation of a wolf pack is more likely. Conversely, if a corporation has a multiple voting share structure, the formation of a wolf pack is less likely,[68] since voting control of the corporation resides with insiders. In other words, regardless of the size of the wolf pack's position, it will always be out-voted by the insider (unless the insider forms part of the wolf pack).[69] As a result, a proxy contest, or the threat of a proxy contest, may be an ineffective means of agitating for change in the corporation.

In addition to a non-controlled (or widely-held) corporation, the presence of an institutional shareholder can facilitate wolf pack formation. The institution by its very presence increases the legitimacy of the point being advocated, and effectively encourages other institutions to join the pack, though it may or may not take on the role of lead activist. Regardless, it is sophisticated and will fulfill a monitoring function, a by-product of which is to allow subsequent members of the wolf pack to free-ride on its efforts. This is especially important in the context of developed capital markets, where larger institutional holders

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Katelouzou, *Myths and Realities of Hedge Fund Activism: Some Emprical Evidence*, 7 VA. L. & BUS. REV. 459, 491 (2013).

[67] Anand & Mihalik, *supra* note 11, at 385-86 (discussing creation of wolf packs to defend against large, monolithic investors).

[68] *See* Bozec, Dia & Bozec, *supra* note 8; *see also* Walid Ben-Amar & Paul André, *Separation of Ownership from Control and Acquiring Firm Performance: The Case of Family Ownership in Canada*, 33 J. BUS. FIN. & ACCT. 517, 518 (2006).

[69] For example, Pershing Square's 2006 activist campaign in respect of Canadian Tire Corporation was halted in its tracks by the daughter of a co-founder of the company, who controlled 61 percent of the company's voting shares through a dual-class structure. Lori McLeod, *U.S. Hedge Fund Kicks the Tire*, CANADIAN HEDGE WATCH (July 4, 2006), http://www.canadianhedgewatch.com/content/news/general/?id=817 [https://perma.cc/7H2C-BWRP].

dominate.[70] In some cases, pension funds—which are usually not at the forefront of shareholder activism[71]—even join together from time to time.[72]

Wolf packs by definition will have a lead who bears the costs of monitoring upfront before convincing other shareholders to join the pack. The lead activist may be willing to bear these monitoring costs upfront because the likelihood of a wolf pack achieving at least one of its intended outcomes is significantly higher than that of an individual activist.[73] It goes without saying, however, that the lead institutional activist is unlikely to begin a campaign for governance reform, especially if the gains are expected to be modest.

The lead activist's position sends a signal to other investors and allows free-riding to occur. By the time it contacts other shareholders, it will have fulfilled at least a portion of its self-chosen monitoring function, thereby allowing subsequent members of the wolf pack to benefit from its efforts. This applies to retail and other similar institutional shareholders. Because institutional investors, such as pension funds, are not generally activists, they may be attracted to a lead activist who has borne (and will continue to bear the bulk of) the monitoring costs upfront. In other words, wolf packs may feature alliances between a hedge fund, as lead activist, and pension funds, and they may be comprised of repeat alliances within the pack.

Shareholders can be incentivized to join a wolf pack because of the opportunity for riskless profit provided by the spike in share price that tends to follow the filing of required disclosure (discussed further below).[74] Even without filing, the lead activist can effectively manufacture a comparable share price

[70] *See generally* John A. Doukas, Chansong Kim & Christos Pantzalis, *Security Analysis, Agency Costs, and Company Characteristics*, 56 FIN. ANALYSTS J. 54 (2000).

[71] For recent statistics on pension fund ownership of Canadian equities, see Vijay Jog & Jack Mintz, *Sovereign Wealth and Pension Funds Controlling Canadian Businesses: Tax-Policy Implications*, *in* UNIVERSITY OF CALGARY SCHOOL OF PUBLIC POLICY: SPP RESEARCH PAPERS 1, 1 (Feb. 2013), https://www.policyschool.ca/wp-content/uploads/2016/03/jogmintz-pensionwealth.pdf [https://perma.cc/236G-BNBA].

[72] *See* Magna International, Inc. (Re) (2011), 34 O.S.C. Bull. 1290 (Can. Ont. Sec. Com.).

[73] Becht et al., *supra* note 59, at 2956 (finding seventy-eight percent success rates for wolf packs compared to forty-six percent success rates for other activists).

[74] In the United States, empirical studies have indicated that Schedule 13D disclosure results in a positive abnormal share price appreciation (even if only in the short-term). *See supra* note 64 and accompanying text. As such, members of wolf packs, with regard to U.S. companies that purchase shares before the lead member of the pack files its disclosure, obtain a riskless profit. *See* Coffee, Jr. & Palia, *supra* note 3, at 593 ("[T]hose who purchase shares in the target firm before the filing of a Schedule 13D and exit at an early point will likely profit handsomely."); *see also* Bebchuk, Brav & Jiang, *supra* note 38, at 1143 (discussing other empirical effects of shareholder activism). To the extent that public knowledge of an activist involvement with an issuer would result in a similar share price appreciation in Canada with the filing of an early warning report, members of the wolf pack have a similar opportunity at riskless profit when the lead member of the pack announces its position.

appreciation by notifying potential members of the wolf pack of its intentions to initiate a proxy contest or agitate for a sale of the target.[75]

In summary, certain conditions give rise to wolf packs. In the absence of these conditions, it may be too costly or impractical for a wolf pack to form. The first condition is a corporation in which the institutional investor is part of the wolf pack. The second condition relates to the lead activist: the lead will assume a monitoring function and will enable other institutions or smaller investors to free-ride, thereby potentially broadening the scope of support for the wolf pack's intervention. The final condition relates to the legal regime in place. Less comprehensive disclosure requirements (including those relating to proxy materials) facilitate wolf pack formation, as discussed in the next Part.

III. LEGAL REGIME

There are no formal rules designed to govern wolf packs *per se*, but their mere formation engages SCG thinking. Are wolf packs, as coordinated groups of sophisticated shareholders, desirable? Do we want to facilitate their formation? While wolf packs form loose networks of investors, they generally seek to accumulate a base of support without triggering the shareholder disclosure obligations that would arise if the group's aggregate position exceeded certain ownership thresholds. This Part examines competing considerations, contemplating whether changes to the legal regime are warranted.

Generally speaking, wolf packs prefer less disclosure to more because of the constraints that transparency places on their formation and behavior.[76] A loose disclosure regime allows wolf packs to outflank corporate defenses, like poison pills, which are triggered when a shareholder or group of shareholders pass an ownership threshold prescribed by the pill. It becomes impossible to trigger the pill when the size of the wolf pack's position is unknown.

In addition, activists can leverage their superior information regarding the size of the pack when engaging the target board.[77] Empirical studies demonstrate that Schedule 13D disclosure is associated with positive abnormal share price appreciation.[78] It is more expensive for a shareholder to purchase shares in a corporation after, rather than before, filing this disclosure; efficient markets

[75] Empirical work has shown that the announcement of a proxy contest is associated with positive abnormal share price appreciation. *See* Lisa F. Borstadt & Thomas J. Zwirlein, *The Efficient Monitoring Role of Proxy Contests: An Empirical Analysis of Post-Contest Control Changes and Firm Performance*, 21 FIN. MGMT. 22, 23 (1992) ("When dissidents fail to gain control, shareholders realize positive abnormal returns over the contest period . . . .").

[76] *See* Wong, *supra* note 62, at 31 (stating that "timely and reliable disclosures constrain the ability of blockholders to secure private benefits").

[77] *Id.* at 28-39.

[78] *See* Bebchuk, Brav & Jiang, *supra* note 38, at 1122, 1125; Coffee, Jr. & Palia, *supra* note 3, at 593.

force large shareholders to buy at prices that reflect their own price impact after the filing, which eats into their returns.[79]

On the one hand, a legal regime that makes it easier for wolf packs to form and requires less disclosure regarding their investments renders it more likely that the monitoring benefits engendered by large blockholders discussed above will materialize. On the other hand, however, rational investors will likely find the mere presence or identity of a wolf pack to be material in making investment decisions. A lenient disclosure regime for wolf packs may allow them to accumulate de facto control blocks without paying other shareholders a control premium, thereby facilitating creeping control acquisitions. These concerns are relevant to (but distinct from) the so-called short-term value maximization as opposed to long-term strategies for the corporation.

In the face of competing valid arguments, should securities law oblige wolf packs to disclose their formation? As is well known, a main rationale for securities disclosure laws generally relates to price efficiency[80]: public issuers and their insiders are mandated to disclose material information so that outside (as well as inside) investors can determine prices for securities that accurately reflect all such information.[81] Further, disclosure reduces agency costs between managers and shareholders; it facilitates monitoring and decreases the likelihood that managers can use corporate assets for self-interested purposes.[82]

The rationale for blockholder disclosure follows a similar logic. It is well-recognized that blockholders can potentially extract private benefits of control, which can impose costs on other shareholders.[83] As suggested above, a lack of blockholder disclosure can also facilitate creeping takeovers where a blockholder is able to acquire a control block from unknowing shareholders without paying a control premium that is typically associated with a takeover bid or other acquisition.[84] A regime requiring blockholders to disclose their respective positions accomplishes at least three objectives, including: protecting against both these risks, allowing other investors to take into account a wolf pack in the investment decision, and reducing the potential costs associated with significant shareholders who exert an undue amount of influence on the corporation for private gain.

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[79] *See* Coffee, Jr. & Palia, *supra* note 3, at 594.

[80] On the efficient markets hypothesis, see generally Eugene F. Fama, *Efficient Capital Markets: A Review of Theory and Empirical Work*, 24 J. FIN. 383 (1970).

[81] *Id.* (detailing importance of price efficiency in the public markets).

[82] *See* Paul G. Mahoney, *Mandatory Disclosure as a Solution to Agency Problems*, 62 U. CHI. L. REV. 1047, 1048 (1995).

[83] *See* Michael J. Barclay & Clifford G. Holderness, *Private Benefits from Control of Public Corporations*, 25 J. FIN. ECON. 371, 372 (1989) (arguing that "because the exchange price reflects the value of corporate benefits that accrue to all shareholders in proportion to their fractional ownership, any difference between the block price and the exchange price reflects benefits that accrue to the blockerholder alone . . . .").

[84] Coffee, Jr. & Palia, *supra* note 3, at 606 (explaining how wolf pack technique can "effectively outflank" disclosure requirements).

Understanding this threefold rationale for enhanced disclosure relating to wolf packs, and the necessary limitations on SCG, indicates how if at all the attending legal regime should be reformed. When shareholders form de facto blocks to exert influence in the corporation and are able to avoid disclosure rules simply by avoiding the characterization of their behavior as joint action, their behavior should be scrutinized. In particular, wolf packs should be regulated like blockholders and be subject to early warning reporting when their collective interest rises above ten percent.[85] Investors who are not part of the wolf pack should have access to all material information including the existence of a wolf pack.

A key question, of course, is what conduct have courts interpreted to be "joint" action? The judicial posture has traditionally been one of restraint. As one court recently stated, "the surgery should be done with a scalpel, and not a battle axe."[86] In one of the few cases dealing with the scope of what behavior qualifies as "acting jointly or in concert" in the context of a proposed proxy contest, a court refused to bar the wolf pack's members from voting their shares despite holding that the wolf pack breached its disclosure obligations; instead, the court ordered the wolf pack to make appropriate disclosures regarding its joint action and delayed the annual general meeting of the shareholders until the shareholders had adequate time to review such disclosures.[87]

Taking a different direction, the U.S. Court of Appeals for the Second Circuit has held that three shareholders were not acting as a group,[88] even though one shareholder "was a well-known raider and all three discussed among themselves how to improve the value of the target company."[89] If this type of thinking becomes widely adopted, wolf packs may be able to extract the private benefits associated with a block position. There is an inherent unfairness in this result

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[85] As the Canadian Securities Administrators noted, "[T]he mere identity and presence of an institutional shareholder may be material to some investors." *CSA Notice and Request for Comment: Proposed Amendments*, ONTARIO SEC. COMMISSION (2013), www.osc.gov.on.ca/en/SecuritiesLaw_mi_20130313_62-104_take-over-bids.htm [https://perma.cc/4JBE-JK57].

[86] Genesis Land Dev. Corp. v. Smoothwater Capital Corp., 2013 ABQB 509, para. 69 (Can.) (citing 820099 Ontario Inc. v. Harold E. Ballard Ltd., [1991] O.J. No. 1082 (Can. Ont.)).

[87] *Id.* at paras. 2, 70-71.

[88] *See* Hallwood Realty Partners, L.P. v. Gotham Partners, L.P., 286 F.3d 613 (2d Cir. 2002).

[89] *See* Coffee, Jr. & Palia, *supra* note 3, at 568; *see also* meVC Draper Fisher Jurvetson Fund I, Inc. v. Millenium Partners, L.P., 260 F. Supp. 2d 616 (S.D.N.Y. 2003); Yucaipa Am. All. Fund II, L.P. v. Riggio, 1 A.3d 310, 329, 360 (Del. Ch. 2010) (holding that rights plan can validly treat as beneficially owned all shares owned by those who joined together to jointly propose and fund proxy contest, and analyzing behavior of two funds and whether acting jointly); Carmen X. W. Lu, *Unpacking Wolf Packs*, 125 YALE L.J. 773, 777-80 (2016) (discussing how wolf packs can evade section 13D); William R. Tevlin, *The Conscious Parallelism of Wolf Packs: Applying the Antitrust Conspiracy Framework to Section 13(D) Activist Group Formation*, 84 FORDHAM L. REV. 2335, 2340-46 (2016) (discussing hedge funds and wolf pack tactic).

and, therefore, joint action should be interpreted and applied broadly to cover a wide range of communication and behaviors associated with wolf pack formation. Future decisions should consider that wolf packs should not be permitted special status in the "acting jointly or in concert" analysis, especially in light of the potentially weak remedies imposed on them for non-compliance.[90]

Of course, the foregoing discussion of the relationship between disclosure and wolf packs leads us to an analysis of insider trading and tipping. The chance at riskless profit engendered by wolf pack members who exchange confidential information runs contrary to the policy animating insider trading and tipping laws which is to protect investor confidence in the marketplace as a level playing field.[91] If existing law makes tipping by persons or companies contemplating take-over bids[92] illegal because of the premium such bids typically command at the announcement,[93] then we can legitimately question whether relationships among wolf pack members fall within the rules prohibiting insider trading and tipping. One might expect that tipping by the lead member of the wolf pack to other investors regarding the lead's plans in relation to the target may also qualify as joint conduct, though the law has not moved in this regard.[94] Securities regulators should similarly consider whether and in what circumstances tipping rules should apply to wolf packs, another form of change of control.

A regulatory regime that acknowledges the reality of SCG must also attend to the potential dangers that emerge when blockholders act collectively as a wolf pack. This is normatively consistent with SCG, the goal of which is to strike a balance between the interests of those shareholders who are empowered to operate as activists and those who hold shares without playing an active role in the corporation.

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[90] *See* Coffee, Jr. & Palia, *supra* note 3, at 563-66.

[91] National Policy 51-201 Disclosure Standards, (2002) 25 O.S.C. Bull. 4492 (Can. Ont. Sec. Com.).

[92] *See* Securites Act, R.S.O. 1990, c S.5, P.76(3) (Can.) (prohibiting tipping).

[93] And, in any event, both would be expected to have significant impacts of the value of a given company's securities.

[94] *See* Coffee, Jr. & Palia, *supra* note 3, at 565 ("[T]ipping and informed trading appears to characterize both the formation of the 'wolf pack' and transactions during the window period preceding the filing of the Schedule 13D."). The practice of tipping in proxy contests is not explicitly illegal unless the actions arise out of an agreement. *See id.* at 566. The standard is murky as to what an agreement means—i.e. a phone call from one wolf pack member to another saying, "I hope I have your support in this proxy fight" is probably okay. However, if the wolf pack member being solicited affirms their intention to support the proposal on that call, then you may have a coordinated agreement and be classified as a "group." Thus they would run afoul of the disclosure rules in Schedule 13D. A shareholder is in a group if it "agree[s] to act together for the purpose of acquiring, holding, voting or disposing of" a company's stock. 17 C.F.R. § 240.13d-5(b)(1) (2018). So, wolf pack members are likely careful to conduct their activities just short of an express agreement. Essentially, the issue has been looked at by the SEC, but the current regime still employs this agreement standard.

CONCLUSION

This Article represents a first step towards understanding the concept of SCG and does so in the context of wolf pack activity. As the law currently stands, wolf packs occupy the role of a blockholder in the corporation, but without the same disclosure obligations that blockholders are required to observe. While a legal regime that facilitates wolf pack formation may make it easier for shareholders to monitor management and thus reduce agency costs in changes of control, these benefits should not come at the price of deficient disclosure. If a sound disclosure system is the cornerstone of securities regulation, then novel tactics aimed at circumventing that system—especially when analogous shareholders are caught by it—should be more comprehensively regulated.