NEW EVIDENCE ON THE EFFECTIVENESS OF THE PROXY MECHANISM

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Abstract

The proxy fight literature to date has focused exclusively on proxy fights that progress to a shareholder vote or near-shareholder vote stage. In contrast, this paper uses a sampling methodology which retains all cases where a proxy fight is threatened, whether or not a vote eventually occurs. Less than one half of threatened proxy fights ultimately result in a shareholder vote. Votes are avoided in three-fourths of dropped contests when the target firm agrees to be acquired, reaches a settlement with the dissident, or restructures to the dissident's satisfaction. These avoided contests are associated with significant increases in target firm value, comparable to the increases observed when contests end with a shareholder vote. The increases in firm value are found to be highly concentrated among firms which are acquired subsequent to a threatened proxy fight, providing evidence that the threat of a proxy fight is most effective as a means of forcing the sale of target firms.

1. Introduction

While there is consensus in the literature that fighting management through a proxy contest is costly and difficult,[1] there is less consensus as to the benefits of such contests to shareholders of target firms. Berle (1962) calls proxy fights "singularly uninspiring as a rule," believing that most contests are "quite obviously a sheer struggle between two tycoons for power." If management decisions are independent of board structure, and dissidents compete solely for the right to run and extract resources from the target firm, then proxy contests would presumably have no positive, and possibly a negative impact on share prices.[2] Manne (1965), conceding that a "small fraction" of control fights represent dissident interest in extracting firm resources, asserts that the primary motivation is poor managerial performance and the resulting opportunity for capital gains. He predicts permanent increases in firm value surrounding proxy fights where dissidents gain control.

Empirical studies consistently find large and significant increases in firm value (abnormal returns) around announcement of a proxy fight, seemingly supporting Manne's hypothesis. Dodd and Warner (1983) find that these increases occur regardless of contest outcome, and therefore argue that proxy fights may discipline incumbent management even when dissidents gain no board seats. DeAngelo and DeAngelo (1989) find that nearly all of the observed increase in firm value for their sample of proxy contests is attributable to firms which are acquired as a result of dissident activity, implying that proxy contests are most beneficial in facilitating the

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[1] Berle and Means (1932) write "the difficulty and cost of dislodging the management, however, emphasizes the precarious nature of control resting on the ownership of a minority of the voting stock." Manne (1965) calls proxy fights the "most expensive, the most uncertain, and the least used of the various techniques" at gaining corporate control. Pound (1988) tests and confirms several factors which discourage the use of proxy contests, including: inefficiency in the system of vote solicitation, conflict-of-interest pressures on institutional investors, and signalling costs of dissidents.

[2] This point is noted by Dodd and Warner (1983).

restructuring of the target firm, or settlement between the target firm and the dissident.

Returns to target firm shareholders surrounding announcement of a proxy contest are large and significant. Market-adjusted returns are a significantly positive 10.51% from 40 days before contest announcement through outcome announcement when no shareholder vote occurs, insignificantly greater than the 9.60% gain when a vote occurs. Increases in firm value are insignificantly positive in the subset of firms where a settlement is reached between the target firm and the dissident, and insignificantly negative when the contest is dropped for another or an unknown reason. The positive returns when a proxy fight is dropped are concentrated among firms which are acquired or restructured, consistent with DeAngelo and DeAngelo's (1989) findings for proxy contests.

In the years following announcement of a proxy contest, there is little evidence of a downward drift in abnormal returns. Market-adjusted returns are fairly steady in the five years following contest announcement both when there is and is not a shareholder vote. When abnormal returns are calculated using Ibbotson's (1975) RATS methodology, which compensates for systematic risk, the returns appear to drift down in the subsample where a shareholder vote occurs, although the decline is statistically insignificant. Significant market-adjusted (RATS adjusted) returns of -19.36% (-21.73%) over months 1 to 24 relative to contest announcement are found, however, for the subsample of firms where the dissident obtains board representation. Ikenberry and Lakonishok's (1993) findings are thus partially replicated on a broader sample of firms, but evidence in this paper suggests that the value gains observed in the full sample of proxy contests are permanent.

The paper proceeds as follows. Section 2 discusses how the sample of threatened proxy

contests is collected. Section 3 discusses the event study methodologies used to examine stock price performance. Section 4 examines the event study results in aggregate as well as in cross section, and section 5 concludes.

2. The Sample

The sample of threatened proxy contests is collected from Mead Data Central's Nexis database. The database is first screened for newspaper stories between January 1, 1977 and December 31, 1988 containing the words: proxy fight, proxy battle, proxy contest, proxy solicitation, consent solicitation, solicit proxies, soliciting proxies, or solicitation of proxies.[4] From these articles, a list of NYSE- and AMEX-listed firms that were potentially the target of a threatened proxy contest is assembled. Newspaper and wire stories from the database are then examined for each of the potential sample firms to determine if a proxy contest was indeed threatened. A threat is deemed to occur if a dissident (or dissidents) publicly states an intention to launch a proxy contest or consent solicitation, or otherwise expresses interest in gaining board control or obtaining a list of shareholders. Threats that are not made publicly are excluded.[5]

Newspaper and wire stories from Nexis are then used to determine the type of proxy contest threatened, the dissident, dissident ownership in the target firm, the outcome, and announcement days. The contest announcement day is defined as the first day in which a

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[4] The number of newspapers covered in the major newspapers (MAJPAP) file of the database expands over the 1977 to 1988 period. *Wall Street Journal* abstracts and *New York Times* abstracts or full text stories are available for the entire sample period, and *Washington Post* stories are first available during 1977. Stories from other major papers are available beginning at various times throughout the 1980s.

[5] Threats made privately to management that are publicly revealed months or years later are therefore excluded, as are cases where management accuses a dissident (or alleged dissident) of launching an illegal proxy solicitation (but there are no dissident statements confirming a proxy solicitation). Similarly, threats that were reportedly made publicly are excluded if the first mention the study finds of the threat appears months or years later.

takeover of target firms.

The value increasing benefits associated with proxy contests are called into question by recent evidence on the performance of target firms in the years following a contest. Ikenberry and Lakonishok (1993) find that target firms exhibit large and significant negative abnormal returns in the two year period following a proxy contest, more than offsetting the announcement period increases in abnormal returns. Interestingly, they find this poor performance concentrated among firms where dissidents successfully obtain board representation. Van Heeckeren (1993), however, examining proxy contest targets from the 1950s, finds significantly positive returns in the years following a contest, regardless of outcome.

The usual empirical methodology used in assessing the effectiveness of proxy fights has been to obtain a sample of cases where a proxy fight occurs, and examine stock price and possibly accounting data surrounding these transactions. An important subset of transactions that are largely missed by these empirical studies, however, are cases where proxy fights are threatened but not carried through to completion.[3] Studying these transactions can lead to a better understanding of the effectiveness of the proxy mechanism.

In examining the full sample of threatened proxy contests, this study finds that less than one half (79/185) go to a shareholder vote. In those cases where no vote occurs, the target firm is acquired 21% of the time, a settlement is reached 48% of the time, and the target firm restructures 5% of the time. In only 26% of abandoned proxy fights is there no acquisition or

[3] These studies often include proxy fights which are settled late in the process (after a contested shareholder meeting date has been set), but exclude threatened proxy fights which do not progress so far. Nine percent (9/96) of proxy contests examined by Dodd and Warner (1983) are settled before the contested meeting, as are 24% (24/100) of the contests examined by Pound (1988), and 26% (25/95) of the contests examined by Ikenberry and Lakonishok (1993).

newspaper or wire story appears reporting the threatened proxy contest. The outcome announcement day is defined as the first day in which a newspaper or wire story appears reporting the outcome of the shareholder vote, or an event which ends the possibility of a contested shareholder vote.[6]

Of the 229 threatened proxy contests for board representation or control, 12 are dropped as the dissident was a labor or consumer advocate,[7] and 32 are dropped because there was a threat within the preceding five years for that firm. The final sample therefore consists of 185 threatened proxy fights for 181 different NYSE- and AMEX-listed firms between 1977 and 1988.

Outcomes of the threatened proxy contests are presented in table 1. Of the 79 contest which reach a shareholder vote, managers win 52% (41/79) of the time, dissidents win 34% (27/79) of the time, and a split victory occurs 13% (10/79) of the time. Other studies have found similar distributions of proxy contest outcomes.

Of the 106 contests which are dropped prior to a shareholder vote, three-fourths of the contests (78/106) are ended by the target firm being acquired, settling with the dissident, or restructuring. Acquisitions of the target firm account for 21% (22/106) of the dropped proxy fights. Most of the acquisitions (15/22) are undertaken by third parties, although 6 of 22 involve the dissident, and 1 of 22 involves target firm management. Settlement agreements between the target firm and the dissident comprise 48% (51/106) of dropped contests. Most settlements (27/51) involve the dissident being granted board representation, but a targeted repurchase of the

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[6] The outcome announcement date is assumed to occur one year after the contest announcement date in 8 contests where an outcome announcement date could not otherwise be determined.

[7] These contests are excluded (following precedence in the literature) as the motivation for these contests seems to differ systematically from that of contests led by other dissidents.

dissident's shares is arranged in a large minority (17/51) of settlements. Restructurings of the target firm by incumbent management accounts for 5% (5/106) of the dropped contests.[8] The remaining 26% (28/106) of dropped contests are not carried out for another or an unknown reason.

The high proportion of threatened contests in which management settles with the dissident, restructures, or agrees to be acquired, suggests that proxy threats are taken seriously by management. Threatened proxy contests do not appear to represent costless jawboning that can safely be ignored by target firm management. This evidence, combined with the relatively high number of contests where no shareholder vote occurs, suggests that dropped proxy contests are potentially important in understanding the effectiveness of the proxy mechanism as a whole.

Descriptive statistics on the proxy contests are provided in table 2. Sixty-nine percent (127/185) of the full sample of contests are for control of the target firm's board, and 31% (58/185) are for representation.[9] Fifty-eight percent (46/79) of contests where a shareholder vote occurs are for control, comparable to what other studies have found. A greater proportion of the contests where no vote occurs are for control (76%), at least partially because dissident statements are often vaguer in this subsample, and press reports less comprehensive.

At contest announcement, mean (median) dissident ownership in the full sample of target

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[8] In some cases the dissident does not reveal the reason for dropping the proxy contest, but the timing of events suggests that the target firm restructuring is a factor.

[9] In control contests, dissidents seek at least 50% of the target firm's board seats, while in participation contests the dissident seeks less than 50% of the target firm's board seats. The study includes five contests where the initial dissident threat concerned board structure, but where the contested shareholder vote was not over board structure, and five contested shareholder votes over board structure where the initial dissident threat did not concern board structure. The table 2 numbers refer to the type of board structure contest first revealed by the dissident. In several instances (once where a shareholder vote occurs, 8 times where no shareholder vote occurs) where the type of contest threatened is unclear, it is assumed that the contest is for control.

firms is 11.9% (8.7%). Dissident ownership is slightly greater when a shareholder vote occurs than when a proxy contest is dropped, with mean (median) values of 12.2% (8.7%) and 11.7% (8.0%) respectively. By outcome announcement, mean (median) dissident ownership increases to 13.5% (9.9%) when a vote occurs and 13.4% (9.4%) when no vote occurs (figures not in table 2), statistics very close to what other proxy contest studies have found.

The 185 threatened proxy fights involve 151 distinct dissidents or dissident groups. The most frequent dissidents, listed in table 2, are popularly known due to their involvement in a variety of corporate control activities. The proportion of contests that go to a shareholder vote for these frequent dissidents, 44% (14/32), is almost identical to the proportion of all contests which go to a shareholder vote (43%).

The last part of table 2 notes the number of threatened proxy contests by year. There are a greater number of threatened fights in the later part of the sample period, due to an increased number of threats which are not carried through to a shareholder vote. This increase may be due to the sample selection method used which results in somewhat better press coverage in the later part of the period.[10]

Table 2 may be most interesting in showing the similarity between proxy contests which result in a shareholder and proxy contests where no vote occurs. The similarity of dissident ownership, and evidence of dissidents who participate in both types of contests suggests that the subgroups of contests are drawn from similar distributions. Further evidence is thus provided that proxy fights which are dropped are important to understanding the overall effectiveness of proxy contests.

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[10] See footnote 4.

3. Research Methodology

An event study methodology is employed using monthly and daily data from the Center for Research in Security Prices (CRSP) where event month 0 refers to contest announcement month and event day 0 refers to contest announcement day. Abnormal returns are calculated using the market-adjusted approach, which makes no control for risk, and Ibbotson's (1975) RATS (Returns across Time and Securities) approach, which allows for time-varying systematic risk. Market-model returns, where parameters are calculated over some estimation period, are commonly used in the literature (Dodd and Warner (1983), DeAngelo (1988), and DeAngelo and DeAngelo (1989)). Ikenberry and Lakonishok (1993) detail the bias that can be introduced with the market model, however, when firms are suffering from systematically poor performance over the estimation period. The market-adjusted approach and Ibbotson's RATS approach are free of this potential bias.

Market-adjusted returns are calculated by netting market returns out from sample firm returns. The abnormal return for each firm i in period t, AR_{it}, is:

$$AR_{it} = R_{it} - R_{mt}$$

where R_{it} is the return to firm i in period t and R_{mt} is the return on the CRSP equal weighted index in period t. For monthly data, the mean return in each time period t is computed, and mean returns are summed to produce a cumulative mean abnormal return. Standard errors are then calculated following Brown and Warner (1980) and are estimated over event months -36 to -3. For daily data, the cumulative abnormal return for each security i is computed, and these cumulative returns are then averaged to compute a mean cumulative abnormal return. Standard errors are calculated using the standardized prediction error approach detailed in Patell (1976)

and Dodd (1980), using event days -250 to -61 as the estimation period.[11]

As calculations of abnormal returns over long periods are sensitive to the methodology employed, monthly data is also analyzed using Ibbotson's (1975) RATS methodology, used in Ikenberry and Lakonishok's (1993) proxy contest study. An event time cross-sectional regression is run for each month t:

$$R_{it} - R_{ft} = \alpha_t + \beta_t(R_{mt} - R_{ft}) + \varepsilon_{it}$$

where R_{ft} is the risk free rate of return in period t, and R_{it} and R_{mt} are defined as above.[12] The intercept α_t is an estimate of the abnormal return in month t, and the cumulative abnormal return is the summation of the time series of α_t. The standard errors used to compute t-statistics for α_t are simply the standard errors from the regressions.

4. Results

A. Preannouncement Monthly Abnormal Returns

Manne (1965) argues that poor managerial performance will reflect itself in poor stock price performance in the period preceding a corporate control bid. The empirical evidence on this point is mixed. Dodd and Warner (1983) and DeAngelo (1988) report insignificantly negative market model returns in the period preceding announcement of a proxy contest. Ikenberry and Lakonishok (1993) find significant (at the .01 level) size and beta-adjusted returns of -34.42% over event months -60 to -4.

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[11] The analysis with daily data examines time intervals which vary across firms, preventing the use of the more common approach to estimating standard errors detailed in Brown and Warner (1980).

[12] The treasury bill rate from Ibbotson Associates' *Stocks, Bonds, Bills, and Inflation* serves as a proxy for the risk free rate. The rate is calculated monthly as the return on the shortest term treasury bill with a maturity of at least one month.

Table 3 provides mean abnormal returns and cumulative mean abnormal returns for the five year period preceding contest announcement, using the market-adjusted approach (panel A) and Ibbotson's (1975) RATS methodology (panel B). Consistent with Manne's (1965) hypothesis, abnormal returns are found to be significantly negative in the period preceding announcement of a proxy contest. For the full sample of threatened proxy contests, market-adjusted returns are -17.50%, significant at the .05 level, over event months -60 to -3. The market-adjusted returns are very close in the subsamples where a vote does and does not occur, -17.83% and -17.20% respectively, both significantly different from 0 at the .10 level. Evidence of negative abnormal returns preceding contest announcement is stronger, both in magnitude and significance, when using Ibbotson's RATS methodology. Manne's hypothesis regarding preannouncement returns is therefore confirmed for proxy contests where a shareholder vote does not occur, as well as where a vote does occur.

B. Announcement Period Daily Market-Adjusted Returns

Table 4 presents mean cumulative market-adjusted returns from 60 days preceding proxy contest announcement through outcome announcement, and Figure 1 displays cumulative mean market-adjusted returns in the 121 day interval centered around contest announcement. Market-adjusted returns are found to be a significantly (at the .01 level) positive 2.99% over days -1 to 1 relative to contest announcement for the full sample. The returns are 1.88% in the subsample where a vote occurs, and 3.80% where no vote occurs, both significant at the .01 level. Dodd and Warner find lower returns at contest announcement (1.2% over days -1 to 0), while

DeAngelo and DeAngelo (1989) find higher returns (4.85% over days -1 to 0).[13]

Consistent with prior work, abnormal returns are also significantly positive in the days preceding contest announcement. Over event days -40 to -2, market adjusted returns are 10.1%, significant at the .01 level, for the full sample of contests. Returns are 10.6% for the subsample where a vote occurs, and 8.9% for the subsample where no vote occurs, both significant at the .01 level. Evidence presented in other studies (Dodd and Warner (1983) and DeAngelo and DeAngelo (1989)), and casual inspection of press reports in this study, suggests that these returns can be explained by actions of the dissidents prior to proxy contest announcement and/or market expectations of the contest announcement.

After proxy contest announcement, there is a small but significant downward drift in stock prices. For the full sample, market-adjusted returns are -1.93% over event days 2 to 10 (significant at the .01 level), and -2.53% from event day 2 through outcome announcement (significant at the .10 level). In both cases where there is a shareholder vote and where there is no vote there is a significant negative return (at the .05 level) over event days 2 to 10 (-1.62% and -2.16% respectively). Returns from event day 2 through outcome announcement are an insignificant -3.05% when a shareholder vote occurs, and a marginally significant (.10 level) -2.17% when no vote occurs.

Dodd and Warner (1983) find a significant (at the .01 level) and slightly more pronounced downward drift of -4.3% between contest and outcome announcement. They argue that at least part of the downward drift is due to the temporary increase in the value of the vote when a proxy

[13] Since the announcement day in this study is defined as the first day a major newspaper or wire story appears reporting the event, market reaction to this story could initially occur on days -1, 0 or 1 relative to announcement day. In previous studies, which only used the *Wall Street Journal* to determine announcement day, initial market reaction to the story could only occur on event days -1 or 0.

contest is occurring (or expected to occur), as outlined by Manne (1965). While they find that this decline is largely driven by observations from the early part of their sample period (their full sample period runs from July 1, 1962 to January 31, 1978), the evidence here suggests that the phenomenon existed between 1977 and 1988.

In spite of the downward drift in the days following contest announcement, market-adjusted returns from event day -40 through outcome announcement are still 10.51% when no shareholder vote occurs, and 9.60% when a vote occurs, both significant at the .01 level. These returns are somewhat greater than those found by other studies. Dodd and Warner (1983) find market model returns of 8.2% from event day -60 through outcome announcement, and DeAngelo and DeAngelo (1989) find market model returns of 6.02% from event day -40 through outcome announcement.

The large and significant mean increase in firm value when no shareholder vote occurs suggests that dissidents are successful at motivating management to increase firm value. The next section explores in what firms the increase in value is occurring.

C. Exploring the Sources of Value Gains

Manne (1965) asserts that firms with the poorest managerial efficiency pose the greatest opportunity for dissidents who believe that they can manage the firm more efficiently. One might therefore predict an inverse relationship between changes in firm value surrounding announcement of a proxy contest, and changes in firm value preceding the contest period. No linear relationship is found for the periods examined. Correlation coefficients between contest period abnormal returns (market-adjusted returns from event day -40 through outcome

announcement) and abnormal returns over event months -60 to -3, -36 to -3, and -12 to -3 are calculated. The coefficients are .07, -.01, and -.09 respectively, all insignificant at the .10 level.

Table 5 explores the sources of the firm value increases further. Mean cumulative market-adjusted returns of various subsets of the full sample of threatened proxy contest are examined over three intervals: *contest announcement* (days -1 to 1), *outcome announcement* (days -1 to 1), and *contest period* (40 days prior to contest announcement through outcome announcement).

Returns at announcement of a proxy contest are positive, and usually highly significant, regardless of outcome. Returns are insignificantly positive at contest announcement when dissidents win seats in a shareholder vote or when the target firm restructures. Other studies have found significantly positive returns at announcement for contests where dissidents successfully gain representation.

At outcome announcement, returns are negative regardless of outcome when a shareholder vote occurs, although only the management victory decline is significant. The decline for all vote outcomes is somewhat surprising as one would expect a net effect of about zero at outcome announcement given that the announcement is anticipated. Other studies have found positive returns at outcome announcement when dissidents are successful, and negative returns when incumbents prevail.

When a shareholder vote does not occur, returns at outcome announcement are 8.19%, significant at the .01 level, when the target firm agrees to be acquired. Returns are -4.78%, significant at the .01 level, when a settlement is reached between the target firm and the dissident. Target firms where dissidents get board seats as well as firms which arrange a targeted

repurchase both exhibit this significant decline in firm value. Returns are also significantly negative (at the .01 level) when a contest is dropped for another or an unknown reason. Returns are insignificantly negative when the target firm restructures.

For the entire proxy contest period, returns are significantly positive and fairly similar regardless of outcome when a vote occurs. Market-adjusted returns are 9.73% when management wins (significant at the .01 level), 8.85% when dissidents win (significant at the .10 level), and 10.00% when there is a split victory (significant at the .05 level). Dodd and Warner (1983) also find similar returns for dissident and management victories, while DeAngelo and DeAngelo (1989) find negative returns when incumbent management is successful.

When a shareholder vote does not occur, returns are 43.24% over the contest period, significant at the .01 level, when the target firm agrees to be acquired. Restructurings are associated with significantly positive (at the .01 level) returns of 18.13%. When a settlement occurs, returns are an insignificant 3.12% over the contest period. Returns are a marginally significant 6.33% (.10 level) when the dissident gets board representation, and an insignificant -2.54% when a targeted repurchase occurs. When contests are dropped for another or an unknown reason the contest period returns are an insignificantly negative 3.10%. The vast majority of the positive returns seen when no shareholder vote occurs are therefore attributable to target firms which restructure or agree to be acquired.

The middle part of table 2 examines the importance of acquisitions in explaining abnormal returns more explicitly. Thirty-four of the target firms in this study (18.2%) are acquired or liquidated within one year of outcome announcement,[14] 11 when a shareholder vote occurs, and

[14] According to CRSP delistings.

23 when no shareholder vote occurs. Market-adjusted returns are 32.31% (significant at the .01 level) over the contest period for these acquired firms, and 5.27% (also significant at the .01 level) for firms not acquired. Returns are 6.98%, significant at the .01 level, for unacquired firms when a vote occurs, and 3.91%, significant at the .05 level, for unacquired firms when a vote does not occur. The evidence suggests that much of the observed increase in target firm values, particularly when a proxy fight is dropped, is attributable to target firms which are acquired.[15]

DeAngelo and DeAngelo (1989) make a similar conclusion for their sample of proxy contests. They calculate market model returns of 15.16% (significant at the .01 level) between event days -40 and contest outcome for firms that are subsequently sold or liquidated and just 2.90% (significant at the .05 level) for firms that remain independent.

The last subsets of firms examined in table 5 are those with frequent and infrequent dissidents. The subsets are examined to determine if there is a difference in the influence of the two types of dissidents. Such an influence might come from a superior ability of frequent dissidents to influence management (perhaps enhanced or caused by a reputation as a corporate "raider"), superior stock-picking ability, or possibly just a difference in the types of contests undertaken (e.g. value creating contests versus power struggle contests).

Firms are classified as having frequent dissidents if the dissident appear in the full sample at least twice (n=52), and as having infrequent dissidents if the dissident appear in the full sample only once (n=133). Firms with frequent dissidents do perform significantly better in the contest period showing market-adjusted returns of 16.85%, versus 7.47% for firms with infrequent dissidents (both significantly different from zero and each other at .01 level). Examining only

[15] The results are very similar when the cutoff for CRSP delisting due to acquisition is extended from one year following outcome announcement to three years following outcome announcement.

firms not acquired within one year of outcome announcement (results not presented in table 2), firms with frequent dissidents show market adjusted returns of 11.64% (significant at the .01 level), versus 2.90% (significant at the .05 level) for firms with infrequent dissidents, significantly different from each other at the .05 level. The superior performance of firms with frequent dissidents is therefore not explained by an increased probability of takeover.[16]

D. Postannouncement Monthly Abnormal Returns

Market efficiency predicts abnormal returns insignificantly different from zero after contest announcement. Ikenberry and Lakonishok (1993) find, however, that firms subject to proxy contests significantly underperform the market after announcement. Over event months 0 to 24 they find size and beta-adjusted returns of -18.31%, significant at the .05 level, and RATS adjusted returns of -12.87%, significant at the .10 level. Furthermore, they find this negative performance concentrated among firms where dissidents obtain board representation. Ikenberry and Lakonishok (1993) cite Collins and DeAngelo's (1990) findings that analysts systematically overestimate the earnings of firms after a proxy contest where dissidents are successful, as additional support for their stock price performance findings.

This study finds very little evidence of a downward drift in stock prices in the months following announcement for the full sample of threatened proxy contests. Table 6 provides mean market-adjusted returns and cumulative mean market-adjusted returns over the five year period following announcement. Market-adjusted returns are an insignificantly negative 1.50% over event months 1 to 24, and are 2.98% over event months 0 to 24 (both insignificantly different

[16] Differences in performance between target firms with frequent and infrequent dissidents are also independent of whether the proxy contest ended with a shareholder vote or not.

from zero). RATS adjusted returns are -3.90% over event months 1 to 24, and 0.96% over event months 0 to 24.[17]

Abnormal returns are more negative for the subsample where a shareholder vote occurs, but remain insignificant. Market-adjusted returns are -5.08% over event months 1 to 24, and -0.78% over event months 0 to 24. RATS adjusted returns are -8.92% over event months 1 to 24 and -4.75% over event months 0 to 24.

Evidence from this study is more consistent with Ikenberry and Lakonishok's evidence when examining the subset of firms where board representation is obtained (see table 7). For the 65 firms where the dissident obtains board representation, cumulative mean market-adjusted returns are -19.36% over event months 1 to 24, significant at the .05 level. Returns are a slightly more negative -21.73% when calculated using the RATS adjusted approach, also significant at the .05 level. Over event months 0 to 24, market-adjusted returns are an insignificant -13.78%, and RATS adjusted returns are -17.46%, significant at the .10 level.

The negative returns associated with the dissident gaining board representation occur regardless of whether the seats were obtained in a shareholder vote or not. When dissidents obtain board seats without a vote, market-adjusted returns are -24.72% over event months 1 to 24, significant at the .05 level, and -16.15% over event months 0 to 24 (insignificant at the .10 level). When dissidents obtain representation through a shareholder vote, returns are an insignificant -13.95% over event months 1 to 24, and -11.27% over event months 0 to 24. RATS adjusted returns are more negative when a shareholder vote occurs over these intervals, although

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[17] A substantial amount of the positive abnormal returns associated with proxy contests occurs in event months -2 and -1. The intervals presented here begin in event month 0 or 1 as the study is examining post-announcement performance in this section.

the magnitudes and differences are all insignificantly different from zero.

Evidence presented here confirms the findings of Ikenberry and Lakonishok (1993) that significantly negative abnormal returns are seen following proxy contests where dissidents obtain board representation. While the returns for this study's sample are less negative, such a difference could be explained by a difference in sample periods (Ikenberry and Lakonishok's sample period runs from January 1968 through January 1988).

The question remains of why significant negative returns are seen following these contests where dissidents obtain board representation. One possibility is that the market (and dissidents) systematically overvalues this subset of firms. One wonders why this overvaluation would not dissipate over time, however.[18] Another consideration is that the results are being driven by a few observations. An examination of firm returns suggests that at least for this study, the removal of a few observations would be enough to eliminate statistical significance in the observed decline. Finally, the results of a study by Van Heeckeren (1993) on proxy contest targets in the 1950s should be considered. She finds significantly *positive* market model returns in the years following proxy contest announcement, regardless of outcome. While Van Heeckeren (1993) concedes that ex-post selection bias could be an issue in her sample, her results clearly suggest that additional analysis should be done before concluding that the market is valuing target firms inefficiently.

[18] No discernible difference in returns across time was found for the firms where dissidents obtain representation.

5. Conclusion

This study provides new evidence on the extent to which proxy fights are effective at disciplining target firm management. Through a sampling scheme that retains all threatened proxy contests, the study finds that less than one half of threatened proxy contests go to a shareholder vote. In three-fourths of abandoned contests the target firm agrees to be acquired, restructures, or reaches a settlement with the dissident. Gains to target firm shareholders are large and significant when a shareholder vote does not follow a threatened proxy contest, and comparable to the gains seen when contests go to a vote. The majority of these gains are attributable to firms which are acquired within one year of the outcome of the proxy contest. Significantly negative returns are found in the years following contest announcement for the subsample of firms where the dissident obtains board representation. There is little evidence in the full sample of threatened proxy contests, however, that returns are systematically positive or negative in the years following announcement.

Additional work on this topic will explore why some threatened proxy contests go to a shareholder vote while others do not. This is an especially interesting question given the similarity in type of dissident, dissident ownership, and pre-announcement abnormal returns between the subsamples of firms when shareholder votes do and do not occur. One interesting hypothesis to test here is Manne's (1965) proposition that settlements are more likely to occur when information about the ability of the opposing factions is more reliable. Similarly, variables which help Pound (1988) explain the winner of a shareholder vote should be useful in explaining where a vote is more and less likely to occur.

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Table 1

Outcomes for 185 Threatened Proxy Contests of NYSE- or AMEX-Listed Firms between 1977 and 1988

Data from Mead Data Central's Nexis (news) database.

outcome	number	percent of full sample
shareholder vote occurs		
management victory	41	22.2
split decision	10	5.4
dissident victory	27	14.6
winner unknown	1	0.5
sub-total	79	42.7
no shareholder vote occurs		
target firm acquired[a]	22	11.9
settlement[b]		
dissident gets board seat	27	14.6
targeted repurchase of dissident's shares	17	9.2
other	7	3.8
target firm restructures[c]	5	2.7
other/unknown	28	15.1
sub-total	106	57.3

a target firm acquired by dissident in 6 cases, management in 1 case, and a third party in 15 cases.
b excluding settlements where target firm acquired.
c excluding restructurings where target firm acquired or settlement occurs.

Table 2

Descriptive Statistics for 185 Threatened Proxy Contests of NYSE- or AMEX-Listed Firms between 1977 and 1988

Data from Mead Data Central's Nexis (news) database.

	total	shareholder vote occurs	no shareholder vote occurs
type of contest[a]			
control[b]	127	46	81
representation[c]	58	33	25
dissident ownership[de] (in percent)			
mean	11.9	12.2	11.7
median	8.7	9.0	8.0
standard deviation	10.3	11.2	9.7
most frequent dissidents (>2)			
Asher Edelman	7	3	4
Carl Icahn	5	4	1
T. Boone Pickens/Mesa Petroleum	5	2	3
Coniston Partners	3	2	1
Shamrock Associates	3	2	1
Shamrock Holdings	3	0	3
Saul Steinberg/Reliance Group	3	0	3
Burt Sugarman/Giant Group	3	1	2
year of contest announcement			
1977	11	2	9
1978	9	9	0
1979	16	9	7
1980	10	5	5
1981	10	7	3
1982	7	4	3
1983	18	7	11
1984	18	3	15
1985	20	9	11
1986	16	7	9
1987	25	9	16
1988	25	8	17

a at date when contest for board seat(s) is first revealed.
b dissident seeks majority of target firm board seats.
c dissident seeks minority of target firm board seats.
d at contest announcement.
e based on 170 (72/98) observations.

Table 3

Preannouncement Abnormal Returns for 185 Threatened Proxy Contests of NYSE- or AMEX-Listed Firms between 1977 and 1988

Abnormal returns (AR) and cumulative abnormal returns (CAR) in percent in 61 month period beginning 60 months before announcement of proxy contest. Market-adjusted returns are calculated as difference between firm returns and CRSP equal-weighted index. RATS adjusted returns are calculated from a cross-sectional regression using Ibbotson's (1975) RATS methodology. Data from CRSP.

Panel A: Market-adjusted returns

month in relation to contest announcement	all firms		shareholder vote occurs		no shareholder vote occurs	
	AR	CAR	AR	CAR	AR	CAR
-60	1.16	1.16	1.66	1.66	0.76	0.76
-48	0.75	-0.09	0.17	0.46	1.19	-0.48
-36	-1.50	-4.10	-1.10	-0.34	-1.80	-6.92
-24	-0.21	-13.61**	0.27	-10.67	-0.58	-15.82**
-12	0.27	-15.13**	0.39	-15.96	0.19	-14.54*
-3	1.19	-17.50**	3.56**	-17.83*	-0.51	-17.20*
-2	2.04**	-15.46**	0.05	-17.78	3.50***	-13.70
-1	6.12***	-9.34	8.86***	-8.92	4.13***	-9.57
0	5.12***	-4.22	4.30***	-4.63	5.71***	-3.86

Panel B: RATS adjusted returns

month in relation to contest announcement	all firms		shareholder vote occurs		no shareholder vote occurs	
	AR	CAR	AR	CAR	AR	CAR
-60	0.65	0.65	1.80	1.80	-0.73	-0.73
-48	0.75	-1.82	0.04	-0.42	1.21	-3.69
-36	-1.95**	-6.75	-2.22*	-3.40	-1.93**	-10.72*
-24	-0.24	-17.79***	-0.39	-14.96*	-0.12	-20.44***
-12	0.17	-22.07***	0.40	-21.47**	0.04	-22.94***
-3	1.09	-24.60***	3.28*	-23.92**	-0.52	-25.10***
-2	1.97*	-22.63***	0.32	-23.61**	3.45**	-21.65**
-1	5.88***	-16.75**	8.37***	-15.24	4.05**	-17.60*
0	4.86***	-11.89*	4.17***	-11.07	5.39***	-12.20

*** mean significantly different from zero at .01 level (using two-sided t-test).
** mean significantly different from zero at .05 level (using two-sided t-test).
* mean significantly different from zero at .10 level (using two-sided t-test).

Table 4

Market-Adjusted Returns Surrounding 185 Threatened Proxy Contests of NYSE- or AMEX-Listed Firms between 1977 and 1988

Cumulative mean market-adjusted returns (CAR) in percent from 40 days before announcement of proxy contest through one day after announcement of contest outcome. Market-adjusted returns are calculated as difference between firm returns and CRSP equal-weighted index. Data from CRSP.

days in relation to contest announcement	all firms	shareholder vote occurs	no shareholder vote occurs
-60 to -41	1.96**	3.31*	0.97
-40 to -21	3.37***	3.60***	2.42**
-20 to -11	2.37***	3.21***	1.75***
-10 to -2	4.32***	3.79***	4.72***
-1 to 1	2.99***	1.88***	3.80***
2 to 10	-1.93***	-1.62**	-2.16**
11 to 20	-0.35	0.26	-0.81
21 to 40	0.29	0.12	0.42
41 to 60	1.17	1.65	0.81
days -1 to 1 in relation to outcome announcement	-1.44***	-1.36**	-1.50***
2 days after contest announcement to 1 day after outcome announcement	-2.53*	-3.05	-2.17*
40 days before contest announcement to 1 day after outcome announcement	10.12***	9.60***	10.51***

*** mean significantly different from zero at .01 level (using two-sided t-test).
** mean significantly different from zero at .05 level (using two-sided t-test).
* mean significantly different from zero at .10 level (using two-sided t-test).

Table 5

Cross-Sectional Analysis of Market-Adjusted Returns Surrounding 185 Threatened Proxy Contests of NYSE- or AMEX-Listed Firms between 1977 and 1988

Mean cumulative market-adjusted returns (CAR) in percent over three intervals surrounding announcement of proxy contest and announcement of contest outcome for various sub-groups of the full sample of threatened proxy contests. Data from CRSP.

sub-group	contest announcement[a]	outcome announcement[b]	pre-contest announcement to outcome announcement[c]
contest outcome			
management victory (vote)	2.03***	-1.79**	9.73***
dissident victory (vote)	0.44	-0.95	8.85*
split decision (vote)	5.24***	-0.71	10.00**
target firm acquired (no vote)	6.93***	8.19***	43.24***
settlement (no vote)	3.13***	-4.78***	3.12
dissident gets board seat	2.81***	-4.04***	6.33*
targeted repurchase	2.79***	-6.88***	-2.54
other	5.16***	-2.80	4.46
target firm restructures (no vote)	1.77	-1.35	18.13***
other/unknown (no vote)	2.93***	-3.36***	-3.10
acquisition activity[d]			
target firm acquired	5.69***	4.16***	32.31***
shareholder vote occurs	3.74***	-2.24	25.52***
no shareholder vote occurs	6.66***	7.51***	35.70***
target firm not acquired	2.40***	-2.63***	5.27***
shareholder vote occurs	1.57**	-1.21**	6.98***
no shareholder vote occurs	3.05***	-3.78***	3.91**
dissident frequency[e]			
frequent dissident	3.55***	-1.16***	16.85***
infrequent dissident	2.77***	-1.55***	7.47***

*** mean significantly different from zero at .01 level (using two-sided t-test).
** mean significantly different from zero at .05 level (using two-sided t-test).
* mean significantly different from zero at .10 level (using two-sided t-test).

a days -1 to 1 in relation to contest announcement.
b days -1 to 1 in relation to outcome announcement.
c 40 days before contest announcement to 1 day after outcome announcement.
d target firm acquired within one year of outcome announcement in 34 cases, according to CRSP delistings, 11 in which a shareholder vote occured, and 23 in which no shareholder vote occurred.
e frequency with which dissident appears in full sample of 185 threatened proxy contests; frequent dissidents (n=52) appear at least twice, infrequent dissidents (n=133) only once.

Table 6

Postannouncement Abnormal Returns for 185 Threatened Proxy Contests of NYSE- or AMEX-Listed Firms between 1977 and 1988

Abnormal returns (AR) and cumulative abnormal returns (CAR) in percent in 61 month period beginning at announcement of proxy contest. Market-adjusted returns are calculated as difference between firm returns and CRSP equal-weighted index. RATS adjusted returns are calculated from a cross-sectional regression using Ibbotson's (1975) RATS methodology. Data from CRSP.

Panel A: Market-adjusted returns

month in relation to contest announcement	all firms		shareholder vote occurs		no shareholder vote occurs	
	AR	CAR	AR	CAR	AR	CAR
0	5.12***	5.12***	4.30***	4.30***	5.71***	5.71***
1	-1.68	3.44**	-3.69**	0.61	-0.21	5.50***
2	1.80*	5.23***	3.49**	4.09	0.52	6.02***
3	-0.04	5.20**	0.33	4.42	-0.32	5.71**
12	0.01	3.62	0.57	4.73	-0.40	2.67
24	0.48	2.98	1.48	-0.78	-0.28	5.70
36	0.95	7.98	0.30	-1.32	1.46	14.95**
48	-1.03	6.62	-0.03	4.21	-1.76	8.49
60	0.21	0.48	1.70	1.10	-0.86	-0.01

Panel B: RATS adjusted returns

month in relation to contest announcement	all firms		shareholder vote occurs		no shareholder vote occurs	
	AR	CAR	AR	CAR	AR	CAR
0	4.86***	4.86***	4.17***	4.17***	5.39***	5.39***
1	-1.39	3.47**	-3.97***	0.20	0.75	6.14***
2	1.56	5.03***	3.52**	3.72	0.76	6.90***
3	-0.19	4.84**	0.32	4.04	-0.68	6.22**
12	0.28	2.63	1.08	3.33	-0.24	3.06
24	0.41	0.96	0.92	-4.75	-0.28	5.26
36	0.62	4.79	-0.08	-9.35	1.65	15.02*
48	-1.07	4.37	-0.27	-2.25	-1.68	9.55
60	0.09	-1.58	1.97	-6.90	-1.01	1.37

*** mean significantly different from zero at .01 level (using two-sided t-test).
** mean significantly different from zero at .05 level (using two-sided t-test).
* mean significantly different from zero at .10 level (using two-sided t-test).

Table 7

Cross-Sectional Analysis of Abnormal Returns After 185 Threatened Proxy Contests of NYSE- or AMEX-Listed Firms between 1977 and 1988

Cumulative mean market-adjusted and RATS adjusted returns (CAR) in percent over three intervals after announcement of proxy contest for various sub-groups of the full sample of threatened proxy contests. Data from CRSP.

Panel A: Market-adjusted returns

sub-group	months in relation to proxy contest announcement (0,0)	(0,12)	(0,24)
board seat(s) obtained[a]	5.58***	-2.52	-13.78
shareholder vote occurs	2.69	6.38	-11.27
no shareholder vote occurs	8.57***	-11.20	-16.15
control obtained[b]	7.54**	-3.48	-7.94
shareholder vote occurs	-0.12	2.41	2.41
no shareholder vote occurs	15.74***	-9.64	-18.33
no board seat(s) obtained[c]	4.75***	7.05	12.39**
shareholder vote occurs	5.23***	4.12	7.58
no shareholder vote occurs	4.48***	8.89*	15.42**

Panel B: RATS adjusted returns

sub-group	months in relation to proxy contest announcement (0,0)	(0,12)	(0,24)
board seat(s) obtained[a]	4.27*	-6.39	-17.46*
shareholder vote occurs	2.47	3.70	-15.97
no shareholder vote occurs	6.02	-9.20	-10.89
control obtained[b]	6.33	-6.74	-12.72
shareholder vote occurs	-0.05	-4.68	-6.07
no shareholder vote occurs	15.72*	-5.89	-14.43
no board seat(s) obtained[c]	4.78***	7.29*	11.11*
shareholder vote occurs	5.17***	6.20	6.82
no shareholder vote occurs	4.63**	8.65	13.73*

*** mean significantly different from zero at .01 level (using two-sided t-test).
** mean significantly different from zero at .05 level (using two-sided t-test).
* mean significantly different from zero at .10 level (using two-sided t-test).

a dissident obtained board representation in 65 cases, 33 in which a shareholder vote occurred, and 32 where no vote occurred.

b dissident obtained control in 29 of the 65 cases in which representation was obtained, 15 in which a shareholder vote occurred, and 14 where no vote occurred.

c dissident obtained no board representation in 119 cases, 45 in which a shareholder vote occurred, and 74 where no vote occurred.

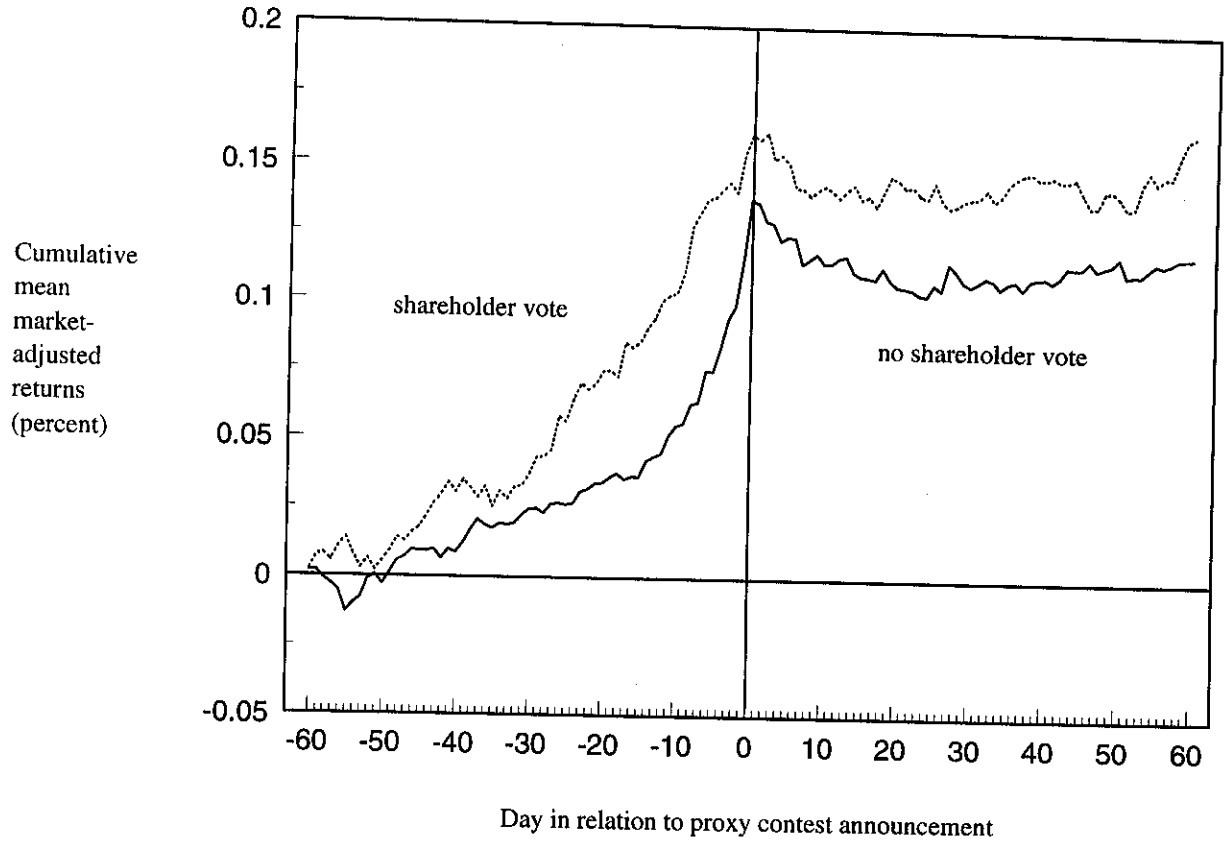

Figure 1. Cumulative Mean Market-Adjusted Returns Surrounding 185 Threatened Proxy Contests of NYSE- or AMEX-Listed Firms between 1977 and 1988. Data from CRSP.