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A New Paradigm for Corporate Governance

Recently, there have been three important studies by prominent economists and law professors, each of which points out serious flaws in the so-called empirical evidence being put forth to justify short-termism, attacks by activist hedge funds and shareholder-centric corporate governance. These new studies show that the so-called empirical evidence omit important control variables, use improper specifications, contain errors and methodological flaws, suffer from selection bias and lack real evidence of causality. In addition, these new studies show that the so-called empirical evidence ignore real-world practical experience and other significant empirical studies that reach contrary conclusions. These new studies are:

Emiliano Catan and Marcel Kahan, *The Law and Finance of Anti-Takeover Statutes*, October 2014

Yvan Allaire and Francois Dauphin, *The Game of 'Activist' Hedge Funds: Cui bono?* August 31, 2015

John C. Coffee, Jr. and Darius Palia, *The Wolf at the Door: The Impact of Hedge Fund Activism on Corporate Governance*, September 4, 2015

For an earlier recognition of these defects in the so-called empirical evidence see, *The Bebchuk Syllogism*.

These new studies provide solid support for the recent recognition by major institutional investors that while an activist attack on a company might produce an increase in the market price of one portfolio investment, the defensive reaction of the other hundreds of companies in the portfolio, that have been advised to "manage like an activist", has the potential of lower future profits and market prices for a large percentage of those companies and a net large decrease in the total value of the portfolio over the long term. *Recognition of the Threat to Shareholders and the Economy from Attacks by Activist Hedge Funds* and *Some Lessons from BlackRock, Vanguard and DuPont—A New Paradigm for Governance*.

Hopefully these new studies will enable and encourage major institutional investors to recognize that they are the last practical hope in reversing short-termism and taming the activist hedge funds. Institutional investors should cease outsourcing oversight of their portfolios to activist hedge funds and bring activism in-house. Short of effective action by institutional investors, it would appear that there is no effective solution short of federal legislation, which runs the risk of the cure being worse than the illness. For an interesting attempt to legislate institutional investor focus on long-term rather than short-term performance see, *European Commission Proposes to Moderate Short-termism and Reduce Activist Attacks*.

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