Comments on Coffee, Jackson, Mitts & Bishop, “Activist Directors and Agency Costs: What Happens When an Activist Director Goes on the Board?”

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December 11, 2017

Fascinating paper!

Comments on Empirics

Main results

- Leakage increases after appointing a director.
  - If the activist is a hedge fund.
  - If the director is an employee of the activist.
  - If there is no confidentiality agreement.
  - The effect disappears within 36 months.
- Bid-ask spread increases after appointing a director.
  - If the director is an employee of the activist.
  - If there is no confidentiality agreement.
  - And only if the activist is a hedge fund?
- Market reaction and option trading relate to settlement type (no tables)
  - Higher returns and lower option trading without employee director
  - Higher returns with confidentiality agreement

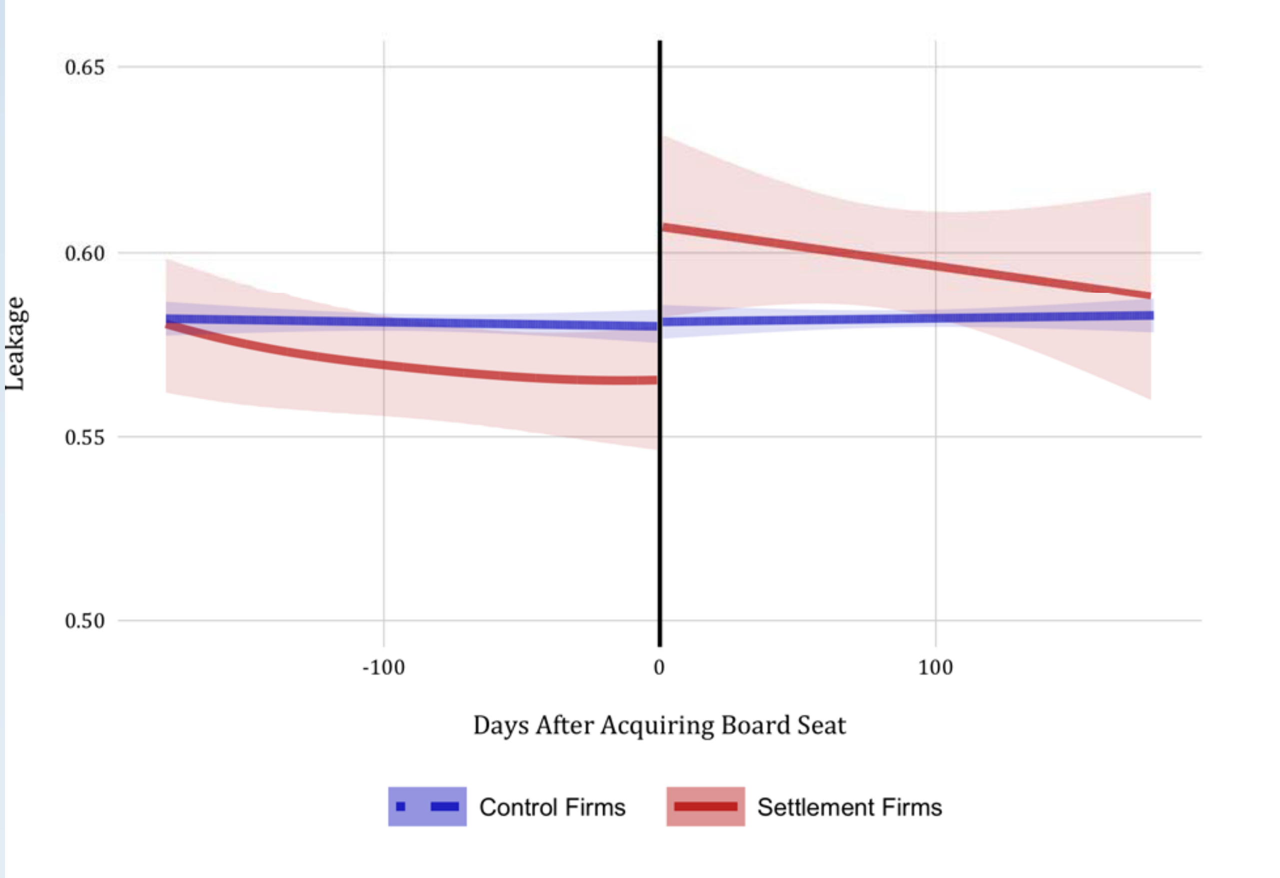

Figure 3: Why does leakage decrease in the 6 months preceding the director’s appointment? Why does it decrease again later?

- The paper says the higher leakage in settling firms disappears as detection risk increases.
  - But detection risk should be highest near director appointment.
  - Detection matters only for illegal trading.
  - Check when the activist sells and when the director resigns.

The gradual disappearance of leakage needs explaining.

Treatment	-0.1350	**	-0.1627	***	-0.1659	***	-0.1742	***
Post	-0.0072		-0.0253	*	-0.0253	*	-0.0241	*
Treatment*Post	0.2064	**	0.2615	***	0.2569	***	0.2535	***
Market Value of Equity Decile			0.0079	**	0.0098	**	0.0089	**
Idiosynchratic Volatility			0.3646		0.3219		0.1841	
Amihud (2002) Liquidity			-0.0175		-0.0200		-0.0156	
Log Book to Market Value			0.0117	**	0.0131	**	0.0132	**
Length of 8-K Filing					-0.0259	**	-0.0130	**
Item Number Fixed Effect	No		No		No		Yes	

Table 5: Treatment firms start with less leakage and catch up after director appointment.

- The dummy variable indicating a firm that settled with an activist (Treatment) is time-invariant.
- If there is a difference of more than a few days between the settlement date and the director appointment date, create a dummy for each.
- Only when the director actually joins the board, can she leak information.

A note on the definition of the treatment group

- Leakage increase only for activism by hedge funds
  - 81% of activists in the sample.
- Leakage increase only for employee directors
  - 70% of directors in the sample.
- Leakage increase only when no confidentiality agreement
  - The majority of settlements in the sample (percentage not reported). Are these agreements enforceable?

Tables 7, 8, 9: Can small sample size explain the absence of an effect for subgroups of treatment firms?

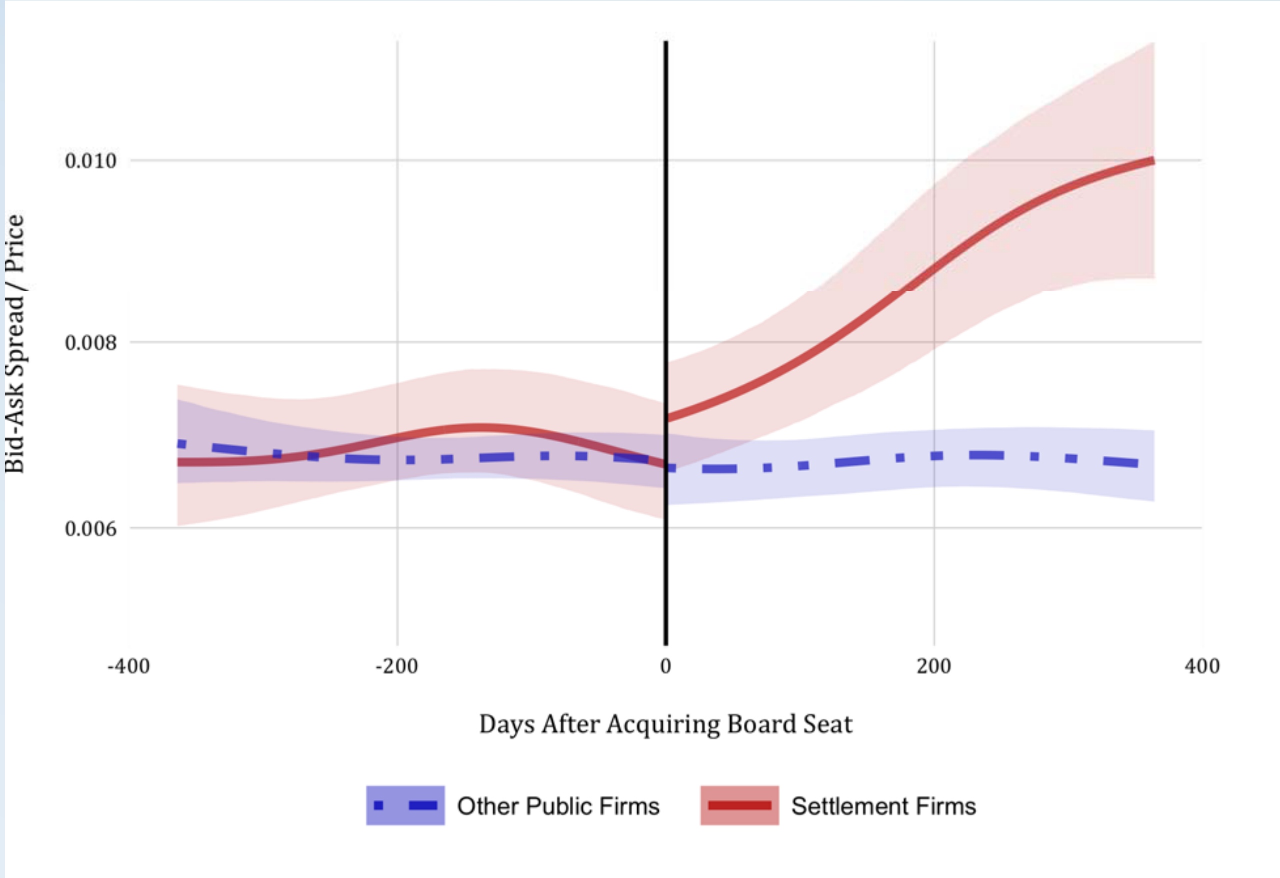

Figure 4: Why does bid-ask spread continue to increase over a year after director appointment (while leakage reverts down)?

- What are the determinants of placing employees on the board?
  - Hedge fund identity; firm characteristics
- Does placing an employee on the board predict the outcome of the activism campaign?
  - This may independently explain the increase in leakage and bid-ask spread.
- Focus on 8-K filings associated with substantial price reactions. Only they contain material information, on which it is illegal to trade pre-filing.
- Include settlement variables also with no interaction with Post in bid-ask spreads regressions (as in leakage regressions)?
  - Treatment in Table 10; Employee Director and Non-Employee Director in Table 11; Information Sharing Rule and Non-Information Sharing Rule in Table 12
- Include firm and year fixed effects?

Miscellanea

Comments on Theory

- The paper says probably not the employee on the board because her trades are easy to trace.
- Trades by her hedge fund employer (the activist) are also easy to trace.
- Still, it is worth checking whether hedge fund employees on corporate boards or their hedge fund employers earn above-market returns after the employee joins the board.

Who trades on inside information when a hedge fund employee is on the board?

- The paper claims they receive tips from the employee on the board in return for supporting the hedge fund that placed her.
  - Can we identify any hedge funds holding stock? Do they earn above-market returns <u>after</u> the employee joins the board?
- The paper argues the tips keeps other hedge funds from selling after the stock price jumps at the filing of the activist's 13D.
  - But they can still benefit from mergers, buybacks, etc.
  - And if tips are needed to keep them, this is a cost of hedge fund activism. Without it the activist's threat will not be credible and the 13D will not affect stock price.
  - Also, it is not clear why the activist would dole out valuable tips, widening bid-ask spread and cutting down its gain, if this is not necessary for its campaign.

The paper says <u>other hedge funds</u> are the traders.

Rule out the possibility that <u>incumbent directors</u> are the traders…

- The paper proposes ways in which institutional investors or the law can combat tipping by hedge fund employees on corporate boards.
- If information sharing (including sharing of non-material information) keeps wolf packs together, preventing it will undermine hedge fund activism. Is this what we want?
- And if the current price of hedge fund activism is too high, the market can fix the problem: hedge fund activists will stop winning board seats, if institutional investors stop backing them.

Do we need a cure?

Thank You