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Engaged's Welling gets early lift with ISS backing at Rovi

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Activist investor Glenn Welling of **Engaged Capital LLC** on Tuesday got a key boost in his short-slate proxy fight at **Rovi Corp.** (ROVI) after a key proxy advisory firm recommended that shareholders back two of three dissident candidates he has up for election to the company's seven-person board on May 13.

Specifically, **Institutional Shareholder Services Inc.**, in a report obtained by The Deal, said that investors should back two dissident candidates. One of the ISS-backed candidates is Welling, who has put himself up as part of his slate. ISS said that Engaged has made a "compelling case for change" and it added that the "alignment" of the two candidates' skills and experience work well with "the challenges the company currently faces."

Not surprisingly, Rovi was disappointed with the result. In a release, Rovi backed its seven directors, noting that its board took deliberate actions to transform its leadership, strategy and structure, and it is "well-positioned" to leverage its compelling patent portfolio and "continue developing next-generation products to drive sustainable returns." The company in March, already under pressure from Welling, expanded its board from six to seven members and added a little new blood in the form of a new director, Steven Lucas, an analytics and technology expert.

Alternatively, Welling said he was "pleased" to receive ISS's endorsement for two directors. "ISS recognized Rovi's need for a fresh, shareholder-focused perspective, relevant and extensive operating experience, and capital markets expertise in the boardroom," he said

The ISS recommendation comes after Welling earlier this year sent a letter to Rovi's directors arguing that shareholder returns have been negative overall since the company was formed by the combination of **Macrovision Corp.** and **Gemstar-TV Guide International Inc.** in May 2008. In the letter, Welling said the board is "long tenured" -- five independent directors have been around since the merger while most have had much longer tenures -- and that new cost management and return on investment expertise is needed.

The Engaged Capital battle takes place after Rovi has experienced three years of protest votes by shareholders against its executive pay packages. The large consistent disgruntled votes against the pay packages may have been a key consideration that helped drive Welling to launch his campaign.

In 2012, only about 70% of voting shares backed the top executive pay packages at Rovi, already a substantial vote of no-confidence. In 2013 Rovi received the backing of just

53% of voting shares. Finally, last year executives received the backing of merely 40%, suggesting that a substantial majority of shares at the time had significant concerns about pay and the performance of the company.

"An activist will target a company if they can establish two things - one, that there is a strong economic thesis for their effort and two that there is a key governance 'hook.' A poor say-on-pay outcome is an objective, highly-visible governance hook," said one corporate advisor.

However, in its report, ISS provided "cautionary" support for shareholders to approve Rovi's 2015 pay packages at the upcoming annual meeting, noting that the company made a number of "improvements to its pay programs that mitigate concerns raised by both the dissident and shareholders." It also said that rising CEO pay and largely time-vested equity awards "warrant continued shareholder monitoring."

ISS also concluded that Engaged Capital has raised "serious questions" about the board's stewardship and its "failure to stem the inexorable loss of shareholder value, relative to peers, over multiple periods."

It also added that Engaged has made a "compelling case" that one of the root-causes of the financial performance problems has been the "board and the management's lack of capital discipline" leading to "failed" M&A transactions that gradually limited the company's financial strength.

While some institutions are expected to vote immediately upon receiving the ISS recommendation, most will make their own internal evaluation and take the proxy advisory firm's recommendations into consideration. In addition, many voters are waiting to see what recommendation will be released by the other major proxy advisory firm - Glass Lewis. That recommendation is expected later this week.