

PHILADELPHIA BUSINESS JOURNAL

VOLUME 25, NUMBER 2

FEB. 24-MAR. 2, 2006

New state law is intrusive, opponents say

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Pennsylvania's new law designed to help Sovereign Bank thwart challenges from dissident investors is a case of politicians needlessly getting involved in private business matters to benefit bank executives at the expense of shareholders, according to industry insiders.



Rendell

"It's unfortunate that the legislature was hoodwinked into believing this was about saving jobs when it was really about protecting the bank's board members," Cohen Brothers & Co. analyst Lee Calfo said.



Scranton

The ultimate impact of the law is being debated in banking circles. Gov. Ed Rendell, who signed the measure into law Feb. 10, warned that it might be too "far reaching" and should be revised. Some question how big of an impact the law will have. Plenty of others, including top

banking executives in the region, don't want to talk about the hot topic.

Senate Bill 595 restricts stockholders' right to oust corporate directors. It also alters Pennsylvania's business corporate law that requires investors with more than 20 percent of a company's stock to buy out other investors who want to sell their stock. The law allows such investors to not count any stock bought through private placement against that 20 percent barrier.

The law is a byproduct of Sovereign's feud with some of its largest institutional investors, who oppose the Wyomissing-based bank's plans to sell 19.8 percent of its stock — \$2.4 billion — to Banco Santander Central Hispano of Spain, and then use the proceeds to help Sovereign buy Independence Community Bank Corp., of New York, for \$3.6 billion. Stockholders such as

Relational Investors and Franklin Mutual Advisors argue that the Santander deal was structured to avoid the 20 percent control proviso from the New York Stock Exchange that would have triggered a Sovereign shareholder vote.

Because there is a kicker in the deal that gives Santander the option to increase its ownership stake to 24.9 percent in a few years, Sovereign sought to alter the Pennsylvania law that would have forced the Spanish banking giant to then purchase other investors' stock at a premium price determined by a judge.

Rendell said he signed the legislation into law to keep Sovereign, the state's second largest financial institution, from moving its headquarters or any of its 4,000 jobs outside of Pennsylvania, as the bank said it would lose state jobs if the deals did not go through.

He was also concerned it may require thousands of other corporations statewide to review and possibly change their bylaws or articles of incorporation. He urged lawmakers to enact new legislation that narrows the impact to just banks.

David Scranton, a banking lawyer at Stradley Ronon Stevens & Young, doesn't understand Rendell's point.

"He's right in that it affects all corporations, but there is nothing in the Sovereign-Santander situation that is unique to banks," Scranton said. "Whichever side you are on in this dispute, issues like the rights of shareholders are relevant to all companies. So I don't see why there is a need for legislation limited just to banks."

Of the more than 10 large and midsize banks contacted in connection with this story, including Sovereign itself and large competitors such as Commerce Bank and PNC Bank, none would comment. The only bank executive to touch this apparent hot potato was Kirk Wycoff, CEO of Continental Bank in Plymouth Meeting.

Wycoff said bank executives should always feel a deep level of responsibility to shareholders.

"If shareholders are going to be diluted, they have a right to vote on it," he said. "That being said I don't know enough about the Sovereign situation to comment specifically about it. I can

say in Sovereign's defense that Wall Street always values short-term gains over long-term profitability.

"But I don't think this new law is going to have a huge effect on other banks because this only affects holding companies and many of them are incorporated in Delaware or elsewhere."

Analysts believe most banks won't have a problem with the new law because it favors management. But none will be affected by the changes unless they face the same issues as Sovereign — dissident investors trying to remove board members and thwart a proposed transaction.

"I am counseling banks to do nothing in response to the law," Scranton said.

Wilson Smith, a Boenning & Scattergood analyst as well as a Sovereign stockholder, is not happy with the new law.

"The whole process was a travesty," Smith said. "It's basically a knee-jerk reaction to put through a bill that completely disenfranchises shareholders. It could help save some jobs in Pennsylvania. But it will have a chilling effect on anyone thinking about holding stock in Pennsylvania companies. ... Do we really want politicians deciding who is going to run the companies in this commonwealth? For the state to involve itself in the ownership of a private company is beyond the pale."

Smith added that board members serve at the pleasure of shareholders.

"Anything else is self-serving crap," Smith said. "Who else has a contract that can't be reviewed? The shareholders have a right to elect whoever they want."

Scranton said when laws are pushed through in a speedy fashion like this one, it often leads to unintended adverse consequences. He said SB 595 could have that chilling effect of which Smith spoke but that it's too early to tell.

"It's conceivable, but it depends on what this actually is," he said. "This [Sovereign situation] could be an aberration or it could be the early stages of shareholders becoming more activist in nature."

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