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The SEC and the Failure of Federal, Takeover Regulation

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THE SEC AND THE FAILURE OF FEDERAL TAKEOVER REGULATION

STEVEN M. DAVIDOFF*

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I. INTRODUCTION

There is a belief that the federal government is on the march in the corporate law realm. The common wisdom is that a reengaged federal government will, at least in some measure, preempt or otherwise regulate corporate matters tradi-

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tionally left to the states. It is evidenced by congressional action in the Sarbanes-Oxley Act and Securities and Exchange Commission (SEC) initiatives.¹ It has spurred some in academia to recast the seemingly eternal race-to-the-bottom/race-to-the-top state corporate law debate into a struggle between the federal government and Delaware.² It has revealed itself in public hand-wringing by Delaware authorities over the possibility, and undesirability, of their reduced role in corporate regulation.³ In short, it is a viewpoint that has become pervasive and consequential.⁴

This worldview is a myth—a bogeyman—when applied to the regulation of takeovers.⁵ Rather, since the late 1980s, the federal government has largely abandoned the takeover business.⁶ True, the SEC alone, and not Congress, has acted quite intermittently since that time to tweak and monitor existing laws and corporate conduct thereunder. But the SEC has not otherwise engaged in any significant rulemaking or otherwise involved itself in the takeover issues of the time. This is true of the periods both before and after the Enron/Worldcom scandals.⁷

The states, led almost exclusively by Delaware, have filled the SEC void, proceeding to oversee, refine, and create new takeover law. Takeover structures, tactics, and strategy have also shifted in response to Delaware's continuing regulation and other market developments. The SEC, however, has not acted to update the federal takeover rules to comport with this substantially altered landscape.

1. See generally Faith Stevelman Kahn, *Bombing Markets, Subverting the Rule of Law: Enron, Financial Fraud, and September 11, 2001*, 76 TUL. L. REV. 1579 (2002) (tracing the development of post-Enron/Worldcom federal reforms); Larry E. Ribstein, *Market vs. Regulatory Responses to Corporate Fraud: A Critique of the Sarbanes-Oxley Act of 2002*, 28 J. CORP. L. 1 (2002) (discussing the substantive parameters of the Sarbanes-Oxley Act).

2. See, e.g., Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588 (2003) (arguing that Delaware is the victor in the race for public corporate charters; its primary competition is now the federal government).

3. See, e.g., William B. Chandler III & Leo E. Strine, Jr., *The New Federalism of the American Corporate Governance System: Preliminary Reflections of Two Residents of One Small State*, 152 U. PA. L. REV. 953 (2003) (discussing the possibility and reality of federal intervention in corporate matters "traditionally" subject to state regulation); E. Norman Veasey, *Musings from the Center of the Corporate Universe*, 7 DEL. L. REV. 163, 163 (2004) (stating that "the Delaware franchise is fragile largely because of encroaching federalization").

4. See, e.g., Stephen M. Bainbridge, *The Creeping Federalization of Corporate Law*, REG. 26 (Spring 2003) (UCLA Sch. of Law, Research Paper Series, Research Paper No. 03-7), available at <http://ssrn.com/abstract=389403> (observing an increasing trend towards federalization of corporate law). The theme of an expansionary federal corporate law is not a new one. See, e.g., Arthur Fleischer, Jr., *"Federal Corporation Law": An Assessment*, 78 HARV. L. REV. 1146 (1965) (observing and arguing for increased federal regulation of securities law).

5. For purposes of this Article, the term *takeover* refers to a transfer of corporate control either by way of tender offer in a transaction or series of related transactions.

6. The academic community has also largely lost interest in federal takeover regulation, and, since the late 1980s, writing on the subject has been limited and sporadic. Compare this to prior periods when it was the "must-write" topic in corporate law. See David W. Leebron, *Games Corporations Play: A Theory of Tender Offers*, 61 N.Y.U. L. REV. 153, 154 (1986) ("The nearly obligatory observation commencing any writing on the subject of tender offers is that no machination of the corporate or financial world has ever attracted greater attention from lawyers, legal scholars, financial economists, or the lay press.").

7. See *infra* Part III (surveying the post-1980s SEC failure to regulate takeovers).

The consequence, this Article argues, is that federal takeover law is currently outdated. It has become inapposite and unsuitable and otherwise fails to regulate today's prototypical takeover. Today we have a federal takeover code that was enacted for a different time and circumstance—an age when the tender offer was newfound, poison pills⁸ and other takeover defenses nonexistent, and other federal takeover regulation, such as antitrust and national security review and waiting periods, virtually absent. This world is lost to time.⁹

The current federal takeover code should therefore, at a minimum, be updated to meet this distinctly new takeover environment; but this Article argues for more. Mere tinkering and one-off rulemaking are insufficient. The magnitude of necessary revision, the piecemeal nature of the existent federal takeover regime, and the interconditionality and cross-dependency of takeover rules alone lead to the conclusion that a sweeping SEC-initiated review of federal takeover regulation is prudent if not essential. In arguing for this sea change, I do not advocate any particular federal takeover norm, merely the application of the SEC's active voice and resources. Historical precedent dictates that anything else should follow quite naturally.¹⁰

But one should not stop there. This Article further argues for the SEC's return to its former role as the nation's primary takeover regulator. This is a throne currently occupied by the Delaware courts.¹¹ Yet this Article finds substantial evidence to support the public choice scholarship of Professor Mark J. Roe and others who argue that the interests of Delaware are narrower and more manager-oriented than the federal government's.¹² The takeover law produced by the Delaware courts in the SEC's absence consequently reflects the state's constricted interests; the code erected may be fine for Delaware but is not appropriate for the diversity of national interests, let alone stockholders. The result is that today we have a Delaware-promulgated takeover code which entrenches management and increases agency costs to the detriment of economic efficiency and stockholder decisional autonomy.¹³

8. For a description of the workings of a poison pill, see John C. Coates IV, *Takeover Defenses in the Shadow of the Pill: A Critique of the Scientific Evidence*, 79 TEX. L. REV. 271, 287 n.62 (2000).

9. See *infra* Part V for further discussion of this temporal mismatch.

10. For a further discussion of the possible outcome of such a review, see *infra* Part VI.A.

11. Here I refer to both the Delaware Court of Chancery and its superior, the Delaware Supreme Court. The Delaware Supreme Court authored the majority of decisions discussed in this Article. But the Delaware Supreme Court reviews only a small number of the takeover-related cases decided in the Court of Chancery, and it almost always affirms its lower court brethren. See Sean J. Griffith & Myron T. Steele, *On Corporate Law Federalism: Threatening the Thaumatrope*, 61 BUS. LAW. 1, 10 (2005) ("The decisions of the Court of Chancery, when reviewed by the Delaware Supreme Court, are most often affirmed."). Given the relative uniformity of decision-making, the two courts can effectively be considered a singular regulator, albeit with slight textual variance and occasional disagreement. They are treated as such in this Article, with any relevant divergence noted.

12. See Mark J. Roe, *Delaware's Politics*, 118 HARV. L. REV. 2491, 2498-2519 (2005). See also Brett H. McDonnell, *Two Cheers for Corporate Law Federalism*, 30 J. CORP. L. 99, 132-38 (2004).

13. See *infra* notes 308-11 and accompanying text for a further discussion of this argument.

Although this Article's call for the federal takeover code's reform should substantially ameliorate these deficits, these failings will quickly reappear if the SEC thereafter remains absent. The Delaware courts will revert to form, again engendering a suboptimal national takeover code. A reengaged SEC will temper, if not stem, this consequence through the SEC's ability to trump, or threaten to trump, Delaware law.¹⁴ It will also bring to bear the SEC's resources and expertise, national rulemaking ability, congressional influence, and bully-pulpit position. These are valuable benefits which the Delaware courts simply cannot institutionally provide.¹⁵ The result will be a more economic, relevant, and coherent national takeover code.

This Article is organized as follows. Part II of this Article highlights the SEC's absence by delineating the SEC's pre-1990s activity in promulgating takeover law and supervising and regulating takeovers.¹⁶ Part III highlights the SEC's post-1989 disappearance as a takeover regulator. Part IV bookends this disappearing act by spelling out the continued rapid course of takeover regulation as the Delaware courts supplanted the SEC as the nation's primary takeover regulator. Part V then examines the failure of federal takeover law in light of the SEC's bowing-out, ongoing state conduct, and the continued evolution of takeovers.

Part VI concludes with a call for an SEC-initiated review of the federal takeover code and an active, engaged SEC as the principal regulator of takeover law. The Part also discusses the federalism issues raised by this proposal as well as its implications for the possibility and appropriateness of wholesale federalization of the nation's takeover code. Although myths can come true, this one should not come to pass. If the SEC is actively engaged, the Delaware courts and the SEC can together create and administer a synergistic national takeover code—one where each body regulates, administers, and collaborates on the takeover issues that correspond to their institutional strengths, albeit with the SEC in a *de facto* dominant position due to its preemptive ability.

Before beginning, an aside on what this Article does not address. This Article is principally occupied with the SEC's conduct, or lack thereof, and not Congress. Historically, Congress acted in corporate matters either at the SEC's behest or, more notably, when scandal hit.¹⁷ For a recent example, recall the congressional furor over the proposed Dubai Ports acquisition.¹⁸ The SEC is the

14. Roe, *supra* note 2, at 2498-99.

15. See *infra* Part VI.B for a detailed discussion of these comparative advantages.

16. Another myth is that the SEC was not an active participant in takeover regulation during this time period. See JOEL SELIGMAN, *THE TRANSFORMATION OF WALL STREET* 589 (3d ed. 2003) (arguing that the SEC's contribution to 1980s takeover regulation was largely "technical").

17. See Stuart Banner, *What Causes New Securities Regulation? 300 Years of Evidence*, 75 WASH. U. L.Q. 849 (1997) (arguing that new, large-scale federal securities regulation is largely the product of scandal or other public furor). See generally Stephen M. Bainbridge, *The Politics of Corporate Governance*, 18 HARV. J. L. & PUB. POL'Y 671, 699-710 (1994-1995).

18. The congressional intervention in the acquisition of Peninsular & Oriental Steam by Dubai Ports and the ensuing political brawl which led to Dubai Ports terminating the

primary federal regulator of the public takeover market. It has a duty to maintain its current regulation, engage in debate of topical and other issues, and propose new legislation to Congress when and where necessary. Congress acts in corporate and securities regulation sporadically at best; the SEC is by design potentially omnipresent. Accordingly, this Article largely concerns SEC conduct, not that of Congress.

II. THE GOLDEN AGE OF FEDERAL TAKEOVER REGULATION

This Part examines federal involvement in takeover regulation during the thirty-year period beginning in the 1960s.¹⁹ A well-respected commentator once described the SEC's involvement in takeover regulation during this time as "quiescent."²⁰ This Part demonstrates that this is not the case. The SEC was instead a significant, and sometimes leading, regulator of the period's consequential takeover issues. Moreover, federal takeover regulation during this era was largely enacted or promulgated piecemeal, tailored narrowly to address the perceived deficiencies of the time.²¹ These observations lay the bedrock for later analysis in this Article concerning the present-day efficacy of federal takeover regulation and the effect of the SEC's subsequent disappearance.

A. *The Williams Act (the 1960s)*

Merger activity in the United States has historically occurred in waves. The "third wave" of U.S. merger activity transpired between 1960 and 1971 and was largely caused by that generation's bubble, the conglomerate acquisition craze.²² At the wave's height, from 1967-69, over 10,000 companies were acquired, with approximately 25,000 firms disappearing throughout the entire period.²³ It

U.S. component of its acquisition is reported in Mark A. Stein, *A Big Deal Overshadowed by the Politics of Ports*, N.Y. TIMES, Mar. 11, 2006, at C2.

19. The goal is not a comprehensive review. This Article therefore excludes wholly from its discussion section 13(d) of the Securities Exchange Act of 1934, as amended (Exchange Act). Section 13(d), added to the Exchange Act by the Williams Act, mandates disclosure of beneficial ownership of more than five percent of a registered class of voting securities within ten days after acquisition of such securities. 15 U.S.C. § 78m(d)(1) (2000). It is an early-warning system with respect to potential unsolicited offers. See generally Peter G. Samuels, *Schedules 13D and 13G: Reporting Beneficial Ownership of Registered Voting Securities*, in SECURITIES FILINGS 2004, at 469 (PLI Corp. L. & Prac., Course Handbook Series No. 2749, Oct. 2004) (setting forth the disclosure and filing requirements of section 13(d)). Though section 13(d) is not discussed herein, it has been a subject of extensive SEC rulemaking since its enactment, providing further evidence of the SEC's regulatory prominence in matters effecting takeovers.

20. SELIGMAN, *supra* note 16, at 583.

21. See Lucian A. Bebchuk & Assaf Hamdani, *Federal Corporate Law: Lessons from History*, 106 COLUM. L. REV. 1793, 1798 (2006).

22. MALCOLM SALTER & WOLF WEINHOLD, MERGER TRENDS AND PROSPECTS FOR THE 1980'S (1980), reprinted in RONALD J. GILSON & BERNARD S. BLACK, THE LAW AND FINANCE OF CORPORATE ACQUISITIONS, at 12, 16-17 (2d ed. 1995). The first wave was from 1897-1904 and consisted primarily of industry consolidating horizontal combinations. See PATRICK A. GAUGHAN, MERGERS, ACQUISITIONS, AND CORPORATE RESTRUCTURINGS 21-26 (2d ed. 1999). The second wave was from 1916-1929 and largely produced oligopolies and consisted of vertical combinations. *Id.* at 26-30.

23. SALTER & WEINHOLD, *supra* note 22, at 17.

was in response to this flurry of activity and the consequent emergence of the cash tender offer that modern-day federal takeover regulation originated. Previously, takeovers were staid events conducted primarily through proxy solicitations regulated by both state and federal proxy law.²⁴ In the mid-1960s, however, at the crest of this third wave, there was a sharp comparative rise in unsolicited or "hostile" takeover attempts.²⁵ These unsolicited bidders typically preferred to evade the federal and state regulatory apparatus applicable to proxy contests and instead often made their takeover attempts via cash tender offer.²⁶ The rise of the tender offer is evidenced numerically: in 1966, there were over 100 tender offers involving companies listed on national securities exchanges as contrasted with just eight in 1960.²⁷

These early tender offers were largely unregulated affairs, and bidder conduct was often egregious.²⁸ The "Saturday Night Special" was a favorite: in one form, a bidder would embark on a pre-offer buying raid to establish a substantial beachhead of ownership at a reduced price.²⁹ This would be followed by a short-period, first-come, first-served public tender offer.³⁰ Disclosure by bidders in these offers was also cramped: target stockholders oftentimes did not know the bidder's future intentions for the corporation, the source or availability of the bidder's capital, or even the bidder's true identity.³¹ In the wake of these new and unfamiliar tactics, stockholders and target corporations were relatively helpless. Takeover defenses at the time were in their infancy and virtually non-

24. See generally EDWARD ROSS ARANOW & HERBERT A. EINHORN, *PROXY CONTESTS FOR CORPORATE CONTROL* (2d ed. 1968).

25. There were 70 unsolicited takeover attempts in the period 1959-1962, compared to 264 attempts in the period 1963-1967. DOUGLAS V. AUSTIN & JAY A. FISHMAN, *CORPORATIONS IN CONFLICT—THE TENDER OFFER* 12 (1970).

26. There were 29 unsolicited tender offers in the period 1959-1962, compared to 41 proxy contests during this time. In the period 1963-1966, the number of unsolicited tender offers rose substantially to 115 tender offers, compared to 63 proxy contests during this time. *Id.*

27. S. COMM. ON BANKING AND CURRENCY, *FULL DISCLOSURE OF EQUITY OWNERSHIP AND IN CORPORATE TAKEOVER BIDS*, S. REP. NO. 90-550, at 2 (1967) [hereinafter *SENATE REPORT*]. The total value of cash tender offers similarly jumped from \$186 million in 1960 to \$951 million in 1965. See Samuel L. Hayes, III & Russell A. Taussig, *Tactics of Cash Takeover Bids*, HARV. BUS. REV., Mar.-Apr. 1967, at 135, 136.

28. See *SENATE REPORT*, *supra* note 27, at 2-4. See generally Arthur Fleischer, Jr. & Robert H. Mundheim, *Corporate Acquisition by Tender Offer*, 115 U. PA. L. REV. 317, 326-27 (1967).

29. The origin of the phrase "Saturday Night Special" is uncertain, but one version has it first employed in 1975, when a public relations executive used the term to malign Colt Industries' unsolicited tender offer for Garlock. See GAUGHAN, *supra* note 22, at 42. An alternative account is that the term arose out of General Cable Corporation's unsolicited offer for Microdot, Inc. See Raymond S. Troubh, *Purchased Affection: A Primer on Cash Tender Offers*, HARV. BUS. REV., July-Aug. 1976, at 79, 86.

30. See Hugh L. Sowards & James S. Mofsky, *Corporate Take-Over Bids: Gap in Federal Securities Regulation*, 41 ST. JOHN'S L. REV. 499, 500-04 (1967) (describing the typical form and structure of a "Saturday Night Special" tender offer).

31. See 113 CONG. REC. 859 (1967); *SENATE REPORT*, *supra* note 27, at 2-6.

existent.³² Indeed, when surveying takeover manuals published during this time period, one marvels at the breadth of subsequent developments.³³

In light of the states' failure to respond, the SEC became the principal governmental actor in the drive to regulate cash tender offers. The SEC, led by its Chairman, Manuel F. Cohen, began a vocal campaign in favor of such regulation and to spotlight abuse.³⁴ The first fruits of the SEC's labor were reaped in 1965, when Senator Harrison A. Williams introduced a bill to regulate tender offers.³⁵ This first bill, however, headlined in the Congressional Record with the portentous title "Protection Against Corporate Raiders," had an avowedly anti-takeover slant. It would, among other things, have required a twenty-day notice period before bidder commencement of a tender offer.³⁶ The SEC, maintaining its activist approach, consequently took a public stance in opposition to many of the provisions of the bill, including the notice period.³⁷

Largely because of this SEC opposition, in 1967 Senator Williams introduced a revised, more neutral bill.³⁸ One of its stated main purposes was "to avoid tipping the balance of regulation either in favor of management or in favor of the person making the takeover bid."³⁹ The final bill, signed into law on

32. Share repurchases and friendly share placements were the two prevalent takeover defenses. See generally David S. Bradshaw, Note, *Defensive Tactics Employed by Incumbent Managements in Contesting Tender Offers*, 21 STAN. L. REV. 1104 (1969) (describing various state-of-the-art takeover defenses circa 1969). In 1967, though, the Delaware courts circumscribed use of share placements by holding them invalid to the extent their primary purpose was to thwart an unsolicited offer. See *Condec Corp. v. Lunkenheimer Co.*, 230 A.2d 769 (Del. Ch. 1967) (invalidating share issuance bestowing corporate control to one of the defendants where primary purpose was to prevent unsolicited tender offer). The Delaware courts were more tolerant of share repurchases, which were generally permissible under Delaware law at the time. See *Cheff v. Mathes*, 199 A.2d 548, 554 (Del. 1964) (applying business judgment rule to uphold stock repurchase so long as it was not "solely or primarily because of the desire to perpetuate [the directors] in office").

33. See, e.g., M. A. WEINBERG, TAKE-OVERS AND AMALGAMATIONS § 2404, at 270 (2d ed. 1967).

34. For example, Chairman Cohen, in the 1968 introduction to the second edition of a prominent treatise on proxy contests, publicly stated that unregulated cash tender offers were "getting away from us." Manuel F. Cohen, *Introduction to PROXY CONTESTS FOR CORPORATE CONTROL*, *supra* note 24, at xvii. See also Manuel F. Cohen, *A Note on Takeover Bids and Corporate Purchases of Stock*, 22 BUS. LAW. 149 (1966); Manuel F. Cohen, *Takeover Bids*, in 2 MERGERS & ACQUISITIONS 87 (1966); Manuel F. Cohen, Chairman, SEC, Address Before the American Society of Corporate Secretaries, Inc., on Proposed Legislation to Regulate Tender Offers (June 28, 1966), in WILLIAM W. BRATTON, CORPORATE FINANCE 1041-43 (5th ed. 2003). The SEC position was particularly noteworthy since there existed strong academic opinion in the period that tender offers were a beneficial force for corporate change and efficient allocation of resources and their regulation would be economically detrimental. See, e.g., Henry G. Manne, *Cash Tender Offers for Shares—A Reply to Chairman Cohen*, 1967 DUKE L.J. 231 (1967).

35. S. 2731, 89th Cong. § 2 (1965).

36. 111 CONG. REC. 28,257 (1965) (statement of Sen. Williams).

37. See SEC. & EXCH. COMM'N, MEMORANDUM TO THE COMMITTEE ON BANKING AND CURRENCY, U.S. SENATE, *reprinted in* S. 2731, 112 CONG. REC. 19,003-06 (1966).

38. S. 510, 90th Cong. (1967).

39. SENATE REPORT, *supra* note 27, at 3.

July 29, 1968, and known as the Williams Act, was almost entirely in the form recommended by the SEC.⁴⁰

The Williams Act itself both substantively and procedurally regulated tender offers, and its terms were keyed specifically to respond to the perceived abuses of the time.⁴¹ First, new section 14(d) obligated bidders to file on Schedule 14D and circulate a disclosure document in connection with a tender offer.⁴² Second, new section 14D attempted to curb coercive practices in tender offers by spelling out substantive governing rules. More specifically, new section 14(d)(5) required a bidder to provide withdrawal rights during the first seven days of the offer and thereafter past the sixtieth day, effectively establishing a seven-day minimum offer period;⁴³ new section 14(d)(6) required a bidder to accept shares tendered during the first ten days of a partial offer on a pro rata basis;⁴⁴ and new section 14(d)(7) required a bidder to offer and pay the same consideration to all tendering stockholders.⁴⁵ Finally, new section 14(e) prohibited misrepresentations, misleading omissions and “fraudulent, deceptive, or manipulative acts or practices” in connection with a tender offer.⁴⁶

The SEC had taken steps to regulate tender offers even before the adoption of the Williams Act. On May 28, 1968, the SEC adopted Rule 10b-4 prohibiting short tendering in connection with a partial tender offer.⁴⁷ The SEC promulgated this rule after congressional statements in Williams Act hearings that the SEC had adequate authority to act.⁴⁸ Thereafter, the SEC speedily moved to im-

40. Pub. L. No. 90-439, 82 Stat. 454 (1968). The SEC eventually had its way even with respect to points of initial divergence between it and Congress. For example, the SEC had recommended that the Williams Act require unlimited withdrawal rights prior to an offer's close. *Full Disclosure of Corporate Equity Ownership and in Corporate Takeover Bids: Hearing on S. 510 Before the Subcomm. on Securities of the S. Comm. on Banking and Currency*, 90th Cong. 23 (1967). In the Williams Act, Congress provided for withdrawal rights only during the first seven days of an offer and thereafter past the sixtieth day. 15 U.S.C. § 78n(d)(5) (1970). But the SEC later acted to steadily expand withdrawal rights to the entire tender offer period. See *infra* notes 84 and 153 and accompanying text. For a legislative history of the Williams Act, see Lyman Johnson & David Millon, *Misreading the Williams Act*, 87 MICH. L. REV. 1862, 1891-95 (1989).

41. Here, I dispute commentators who have termed the Williams Act a weak regulatory response. The Williams Act addressed and regulated the significant concerns of the era. If anything, the Williams Act was viewed by commentators of the time as too strong a medicine. See, e.g., Manne, *supra* note 34. It would only be later developments in takeovers that would recast the Williams Act as a relatively weak legislative act.

42. 15 U.S.C. § 78(n)(d)(1) (1970). Schedule 14D attempted to remedy the information gap in tender offer practice by mandating disclosure of, inter alia, the bidder's plans and proposals for the target, arrangements with any third party with respect to acquired target securities, source and amount of funds, background, and identity. *Id.*

43. *Id.* § 78n(d)(5).

44. *Id.* § 78n(d)(6).

45. *Id.* § 78n(d)(7).

46. *Id.* § 78(m)(e)(1).

47. Adoption of Rule 10b-4 under the Exchange Act of 1934, Exchange Act Release No. 8321, [1967-1969 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 77,558 (May 28, 1968). Short tendering is the tender of securities into a partial offer that the tendering stockholder borrows and does not own. As a result, the number of shares purchased from the stockholder will increase and the number of shares purchased from other investors will be correspondingly reduced. *Id.* at 83,185.

48. SENATE REPORT, *supra* note 27, at 5.

plement the Williams Act and assume its oversight role of takeovers; within a few months of passage, the SEC adopted and then revised emergency implementing Williams Act regulation.⁴⁹ In the revising release, the SEC also put forth an expansive position on the scope of the Williams Act definition of a “tender offer.”⁵⁰ On October 8, 1969, the SEC also adopted Rule 10b-13, which prohibited bidders, from the time of announcement of a tender offer, from purchasing the security subject to the tender offer other than pursuant to that offer.⁵¹ At the turn of the decade, and at the SEC’s behest, the Williams Act was amended by Congress.⁵² The amendments brought exchange offers within the Williams Act’s regulatory compass and provided the SEC with rulemaking authority under section 14(e) “to deal with . . . rapidly changing problems.”⁵³ The amendments also lowered the triggering threshold for the Williams Act’s substantive and procedural requirements from a tender offer for ten percent of a corporation’s equity to five percent.⁵⁴

The framework for future regulation had been set, and the SEC had dived head-first into the takeover regulation business.

B. *Going-Privates (the 1970s)*

The third wave of merger activity subsided in the early 1970s with the popping of the conglomerate stock bubble and repeated U.S. economic recession.⁵⁵ These two events combined to birth the next major issue of takeover regulation: the abusive going-private.⁵⁶ These were largely “take ‘em public high—buy ‘em

49. The issued rules more specifically delineated tender offer disclosure and filing requirements. Adoption of Temporary Rules and Regulations Under Sections 13(d) and (e) and Sections 14(d) and (f), Exchange Act Release No. 8370, [1967-1968 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 77,581 (July 30, 1968); Amendments to Temporary Rules and Regulations Under Sections 13(d) and (e) and 14(d), Exchange Act Release No. 8392, [1969-1970 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 77,715 (Aug. 30, 1968) [hereinafter August 1968 Amendments].

50. The SEC stated that a special bid would thereafter be considered a tender offer subject to the Williams Act. August 1968 Amendments, *supra* note 49, at 83,638. A special bid was a procedure to permit the purchase of large blocks of stock through a fixed price bidding process. See Nathaniel B. Smith, Note, *Defining “Tender Offer” Under the Williams Act*, 53 BROOK. L. REV. 189, 198-99 (1987) (discussing special bids and their unregulated use prior to the SEC’s application of the Williams Act).

51. Adoption of Rule 10b-13 Under the Securities Exchange Act of 1934, Exchange Act Release No. 8712, [1969-1970 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 77,745 (Oct. 8, 1969) [hereinafter Rule 10b-13 Release]. Rule 10b-13 was proposed on the same day that the SEC adopted revised implementing regulations for the Williams Act. Notice of Proposed New Rule 10b-13, Exchange Act Release No. 8391, [1967-1969 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 77,593 (Aug. 30, 1968). In 1999, Rule 10b-13 was amended and redesignated as Rule 14e-5. Regulation of Takeovers and Security Holder Communications, Exchange Act Release No. 42055, [1999-2000 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 86,215, at 82,608 (Oct. 22, 1999) [hereinafter M&A Release].

52. Act of Dec. 22, 1970, Pub. L. No. 91-567, 84 Stat. 1497.

53. 116 CONG. REC. 3024 (1970) (statement of Sen. Williams).

54. 15 U.S.C.A. § 78n(d)(1) (1971).

55. SALTER & WEINHOLD, *supra* note 22, at 18.

56. A going-private transaction, sometimes referred to as a freeze-out transaction, can be defined as a transaction where an affiliate of a publicly held corporation (for example, a member of management or a controlling or substantial stockholder) acquires, or causes to

out low” affairs; controlling affiliates of corporations who had only recently engaged in initial public offerings when stock market prices were substantially higher offered to buy out their own publicly held stock at markedly lower prices.⁵⁷ Because there was an inherently coercive element in these transactions and the opportune timing was at the affiliates’ discretion, these purchases engendered cries of fraud and unjust enrichment.⁵⁸ The states’ response was, at least initially, relatively sluggish,⁵⁹ and the SEC again took the wheel maintaining its role as the nation’s primary takeover regulator.⁶⁰

In 1975, the SEC launched a fact-finding investigation and simultaneously proposed rules to govern going-private transactions.⁶¹ One form of the proposed rule would have required that a price paid in such a transaction be no lower than “the consideration recommended jointly by two qualified independent persons.”⁶² Adoption of this rule was delayed, largely due to allegations that the SEC lacked rulemaking authority under the Williams Act.⁶³ Then in 1977, the

be acquired, the corporation’s remaining publicly traded corporate equity. Consequently, the corporation becomes “private” and its equity is no longer publicly traded. *See generally* Going Private Transactions by Public Companies or Their Affiliates, Exchange Act Release No. 14185, [1977-1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 81,366, at 88,737-38 (Nov. 17, 1977) [hereinafter Going-Private Proposal Release].

57. For an in-depth discussion of the legal controversy surrounding going-private transactions in the 1970s and the scope of claims arising therefrom, see *id.* at 88,736-39; see also Arthur M. Borden, *Going Private—Old Tort, New Tort, or No Tort?*, 49 N.Y.U. L. REV. 987 (1974).

58. There was a profuse amount of academic commentary at the time written on this issue. *See, e.g.*, Borden, *supra* note 57; Victor Brudney, *A Note on “Going Private,”* 61 VA. L. REV. 1019 (1975); Victor Brudney & Marvin A. Chirelstein, *A Restatement of Corporate Freezeouts*, 87 YALE L.J. 1354 (1978); Edward F. Greene, *Corporate Freeze-Out Mergers: A Proposed Analysis*, 28 STAN. L. REV. 487 (1976); Edmund H. Kerr, *Going Private: Adopting a Corporate Purpose Standard*, 3 SEC. REG. L.J. 33 (1975); F. Hodge O’Neal & Ronald R. Janke, *Utilizing Rule 10b-5 for Remedying Squeeze-Outs or Oppression of Minority Shareholders*, 16 B.C. INDUS. & COM. L. REV. 327 (1975); Anne Jentry, Note, *The Developing Law of Corporate Freeze-Outs and Going Private*, 7 LOY. U. CHI. L.J. 431 (1976); Note, *Going Private*, 84 YALE L.J. 903 (1975).

59. The only state to take legislative action was Wisconsin. 13 Wis. Admin. Code SEC § 6.05(1)(a)1-3 (1978). The state court response was also tepid at first; these courts initially reviewed these transactions under a “business purpose” or a modified fairness test which often relegated minority stockholder claims to be remedied, if at all, through appraisal proceedings. This approach was deemed unsatisfactory by many critics. *See generally* Greene, *supra* note 58, at 496-506 (surveying the scope of state decisions prior to 1976 concerning going-private transactions). *But see* *People v. Concord Fabrics, Inc.*, 371 N.Y.S.2d 550 (N.Y. Sup. Ct. 1975) (enjoining going-private transaction under New York law).

60. In a polemical speech made at Notre Dame law school, SEC Commissioner A.A. Sommer, Jr., initiated the SEC charge against going-private transactions. He labeled them as “serious, unfair, and sometimes disgraceful, a perversion of the whole process of public financing.” “Going-Private”: A Lesson in Corporate Responsibility, [1974-1975 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 80,010, at 84,695 (Nov. 20, 1974) (A. A. Sommer, Jr., SEC Commissioner, Address Before the Law Advisory Council Lecture at the Notre Dame Law School (Nov. 1974)).

61. Notice of Public Fact-Finding Investigation and Rulemaking Proceeding in the Matter of “Going Private” Transactions by Public Companies and Their Affiliates, Exchange Act Release No. 11231, [1974-1975 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 80,104 (Feb. 6, 1975).

62. *Id.* at 85,092.

63. *See, e.g.*, Greene, *supra* note 59.

Supreme Court in *Santa Fe Industries v. Green*⁶⁴ overruled the Second Circuit's holding that Rule 10b-5 constituted a basis to challenge a going-private decision on substantive grounds.⁶⁵ This decision, and continued dissatisfaction with state regulation of going-privates—primarily the Delaware Supreme Court's decision in *Singer v. Magnavox Co.*⁶⁶—led the SEC to repropose rules.⁶⁷ These rules were finally adopted by the SEC in 1979, and, although not as far-reaching as originally proposed, established a new disclosure-based regime for going-privates.⁶⁸ Most notably, the rules now obligated corporations in going-private transactions to express an opinion as to the “fairness” of the transaction to unaffiliated stockholders.⁶⁹ The SEC conduct was particularly noteworthy given the view of many that it did not have the legal authority to adopt even this scaled-back regulation.⁷⁰

The other major takeover issue of this decade concerned the scope of the Williams Act. The Williams Act regulated tender offers, but intentionally did not define what constituted a tender offer triggering the Act's substantive and procedural requirements.⁷¹ Not surprisingly, in light of this uncertainty, bidders repeatedly structured their purchases so as to claim that they did not constitute tender offers.⁷² But the SEC was quite energetic in establishing an expansive view of this definition and consequent reach of the Williams Act.⁷³ Immediately

64. 430 U.S. 462 (1977).

65. *Id.* at 474-76.

66. 380 A.2d 969 (Del. 1977). In *Singer*, the Delaware Supreme Court held that a going-private transaction must have a valid business purpose. A transaction “made for the sole purpose of freezing out minority stockholders” lacked such purpose and therefore was “an abuse of the corporate process.” *Id.* at 980. The court further held that even if a valid business purpose was existent, a Delaware court should still “scrutinize the circumstances for compliance with the . . . rule of ‘entire fairness’ . . .” *Id.* at 979-80. Though it did not succeed, *Singer* was arguably Delaware's attempt to forestall SEC rulemaking and was in reaction to the SEC's heated criticism of going-privates. See GILSON & BLACK, *supra* note 22, at 1256 n.40 (arguing that *Singer* was a response to “political considerations”).

67. Going-Private Proposal Release, *supra* note 56.

68. Going Private Transactions by Public Companies or Their Affiliates, Exchange Act Release No. 16075, [1979 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,166 (Aug. 2, 1979) [hereinafter Going-Private Adopting Release].

69. *Id.* at 82,130.

70. See generally Mary-Ellen Hunt, Comment, *An Appraisal of Authority for the Fairness Standard Contained in the SEC's Proposed “Going-Private” Regulations*, 28 EMORY L.J. 111 (1979) (noting criticism of the SEC's statutory authority to regulate going-private transactions). The SEC devoted a substantial portion of the Going-Private Proposal Release to justify the proposed going-private regulations as within its rulemaking authority. Going-Private Proposal Release, *supra* note 56, at 88,740-44. In doing so, the SEC quoted the testimony of Thomas G. Corcoran, one of the authors of the Williams Act, to claim that the Williams Act “was broadly framed to protect investors ‘from exploitation by corporate insiders.’” *Id.* at 88,741. This marked a significant step afar from the neutrality *vis-à-vis* targets and bidders that the SEC had proclaimed in the Williams Act hearings.

71. See Note, *The Developing Meaning of “Tender Offer” Under the Securities Exchange Act of 1934*, 86 HARV. L. REV. 1250, 1250 (1973).

72. See generally Thomas J. André, Jr., *Unconventional Offers Under the Williams Act: The Case for Judicial Restraint*, 11 J. CORP. L. 499 (1986) (outlining various types of unconventional purchases potentially outside the scope of the Williams Act).

73. See Note, *supra* note 71, at 1261-70 (outlining SEC attempts to establish an expansive Williams Act definition of *tender offer*).

upon passage of the Williams Act the SEC published its position on the definitional scope of a tender offer. Then in 1974, the SEC released a notice of a fact-finding investigation to consider issuance of a regulatory definition of a tender offer under the Williams Act.⁷⁴ After hearings, the SEC announced that such a rule was neither “appropriate nor necessary” at that time; rather, abstention would preserve SEC flexibility to respond to developments in transaction types that are or should be encompassed by the term.⁷⁵ For the remainder of the 1970s, the SEC largely pursued its quest in the courts, achieving a measure of success when its eight-factor broad definitional test for a tender offer was adopted in the 1979 case of *Wellman v. Dickinson*.⁷⁶ Shortly afterwards, the SEC attempted to capitalize on this victory by again proposing regulation and legislation further enlarging the tender offer definition to encompass unconventional purchases such as purchases outside the temporal offer period.⁷⁷ None of these proposals, however, resulted in new regulation or law.

The SEC was also acting during this time to refine and broaden the requirements of the Williams Act. On September 9, 1974, the SEC initiated an investigatory proceeding “to develop a factual basis for determining whether it is necessary or appropriate . . . to adopt or amend rules, . . . and/or to recommend further legislation” concerning takeovers and acquisitions.⁷⁸ On August 2, 1976, the SEC proposed a wholesale revision to the takeover code based on the find-

74. Notice of Public Fact-Finding Investigation in the Matter of Beneficial Ownership, Takeovers and Acquisitions by Foreign and Domestic Persons, Exchange Act Release No. 11003, [1974-1975 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 79,956 (Sept. 9, 1974) [hereinafter 1974 Fact-Finding Release].

75. Tender Offers—Notice of Proposed Rules and Schedules, Exchange Act Release No. 12676, [1976-1977 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 80,659, at 86,696 (Aug. 2, 1976) [hereinafter 1976 Tender Offer Release].

76. 475 F. Supp. 783 (S.D.N.Y. 1979), *aff'd on other grounds*, 682 F.2d 355 (2d Cir. 1982). *Wellman* adopted a broad-based, eight-factor test proposed by the SEC itself to determine if a stock purchase or series of purchases constituted a tender offer. *Id.* at 823-24. The standard announced in *Wellman* quickly became the judicial norm for determination of a tender offer under the Williams Act. *See generally* Smith, *supra* note 50, at 201-09 (discussing the *Wellman* test and its adoption by courts in subsequent cases).

77. *See* Proposed Bill to Amend Williams Act, *reprinted in* 542 Sec. Reg. & L. Rep. (BNA) 20 (Special Supplement Feb. 27, 1980); Proposed Tender Offer Rules and Schedule, Exchange Act Release No. 15548, [1979 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 81,935, at 81,229-31 (Feb. 5, 1979) [hereinafter 1979 Proposed Rules and Schedule Release] (publishing for comment proposed tender offer definition); Proposed Amendments to Tender Offer Rules, Exchange Act Release No. 16385, [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,374 (Nov. 29, 1979) [hereinafter 1979 Proposed Rules Release] (withdrawing tender offer definition proposed in 1979 Proposed Rules and Schedule Release and proposing a new definition); Letter from SEC Chairman Harold M. Williams to Senator William Proxmire, *reprinted in* Tender Offer Legislation Proposed [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,453 (Feb. 15, 1980) (proposing tender offer definition encompassing any acquisition of ten percent of a class of equity securities). *See generally* André, *supra* note 72, at 529-33 (discussing the substantive scope of each of the foregoing definitional proposals); James H. Fogelson et al., *Changing the Takeover Game: The Securities and Exchange Commission's Proposed Amendments to the Williams Act*, 17 HARV. J. ON LEGIS. 409 (1980) (reviewing the SEC's legislative recommendations for defining a tender offer under the Williams Act).

78. 1974 Fact-Finding Release, *supra* note 74, at 84,461.

ings of this investigatory proceeding.⁷⁹ These proposed rules would not be adopted, but would form the basis for later rulemaking.⁸⁰ On July 21, 1977, the SEC finally adopted permanent disclosure requirements for Schedule 14D “to replace its emergency rules under the Williams Act” and as part of an effort to adopt a “comprehensive regulatory framework with respect to tender offers.”⁸¹ In 1979, on the same day it adopted going-private rules, the SEC also promulgated rules for the governance of issuer tender offers similar to those for third party offers.⁸²

The SEC finished out the decade by substantially revising the Williams Act rules to principally adopt the 1976 proposed rules.⁸³ The SEC changes effectively eliminated all vestiges of the old “Saturday Night Special” for any and all tender offers: new Rule 14e-1 lengthened the minimum offering period to twenty business days from the *de facto* seven calendar days required by old Rule 14d-5.⁸⁴ Other rules set forth procedures for bidders to compel targets to mail the bidder’s tender offer materials to target stockholders or otherwise provide the necessary stockholder information for mailing by the bidder itself—an alternative to state statutes increasingly perceived as deficient.⁸⁵ Finally, reweighing the state/federal takeover regulatory scales, the SEC also promulgated Rule 14d-2, which required that an offer commence within five business days of announcement.⁸⁶ This SEC action was telling; it directly and intentionally preempted emergent state regulation mandating conflicting pre-approval or waiting periods before commencement of a takeover bid.⁸⁷ In this last deed, the SEC had taken steps to reassert definitively its authority over takeover regulation.

The SEC thus continued its heightened involvement in takeover regulation throughout the 1970s, acting vigorously during this time to preserve its position

79. 1976 Tender Offer Release, *supra* note 75.

80. 1979 Proposed Rules and Schedule Release, *supra* note 77, at 81,207 (withdrawing the 1976 Tender Offer Release and publishing for comment certain proposed rules and a related schedule pertaining to tender offers).

81. Filing and Disclosure Requirements Related to Tender Offer, Exchange Act Release No. 13787, [1977-1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 81,256, at 88,372 (July 21, 1977).

82. Tender Offers by Issuers, Exchange Act Release No. 16112, [1979 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,182 (Aug. 16, 1979).

83. Tender Offers, Exchange Act Release No. 16,384, [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,373 (Nov. 29, 1979) [hereinafter 1979 Tender Offer Release].

84. 17 C.F.R. § 240.14e-1 (1980). Under amended Rule 14d-7, withdrawal rights were extended to an initial fifteen business day period with an additional ten business day withdrawal period required if a competing offer was commenced under certain conditions. *Id.* § 240.14d-7. Rule 14d-8 now permitted bidders to vary the acceptance period for partial offers and extend withdrawal rights for a duration longer than the seven days required by Rule 14d-6. *Id.* § 240.14d-8.

85. 1979 Tender Offer Release, *supra* note 83, at 82,586-89. This rule was again an act by the SEC in the face of criticism that its rulemaking was beyond its authority. *Id.* at 82,587.

86. 17 C.F.R. § 240.14d-2.

87. 1979 Tender Offer Release, *supra* note 83, at 82,583-84. The federal courts acted definitively to adopt the SEC’s position, quickly overturning on preemption grounds conflicting state takeover statutes. *See, e.g., Canadian Pac. Enters. (U.S.) v. Krouse*, 506 F. Supp. 1192 (S.D. Ohio 1981) (holding Ohio takeover regulation requiring precommencement period of twenty days to be preempted by SEC Rule 14d-2).

as the nation's regulator of takeovers and supplant state takeover law where it deemed appropriate.

C. Hostile Takeovers (the 1980s)

The fourth wave of takeover activity commenced in the late 1970s and early 1980s and ended in 1989 in the wake of the collapse of the high-yield bond market and the S&L scandal. The heightened activity was again quantitatively marked: the annual value of acquisition transactions rose from \$43.5 billion in 1979 to a peak of \$246.9 billion in 1988 before bottoming out at \$71 billion in 1991.⁸⁸ Unsolicited takeover activity, mainly cash tender offers, sharply increased from twelve contested tender offers in 1980 to forty-six such offers in 1988,⁸⁹ the increase juiced by cheap financing in the form of high-yield bonds.⁹⁰ But this wave was different in one significant respect: this time targets were equipped for defense. The fourth wave was notable for the wide-spread target resort to takeover defenses, including such colorfully named measures as poison pills, shark repellents, pac-mans, golden parachutes, and greenmail.⁹¹ The renewed vigor of targets, as well as revised bidder tactics, would spur a revolution in takeover methodology, resulting in more extended public takeover battles and leading state courts, state legislatures, Congress, federal courts, and the SEC to confront this phenomenon. The SEC again particularly met this challenge. Although the SEC's involvement in takeover regulation during this period was extensive and reached high tide, the SEC arguably failed to meet many of its announced goals. The remainder of this Part illustrates the breadth of SEC involvement by briefly highlighting three of the main SEC efforts during this era.⁹²

88. SALTER & WEINHOLD, *supra* note 22, at 32.

89. GAUGHAN, *supra* note 22, at 42. The activity was also pervasive, and during this time period thirty percent of the corporations in the Fortune 500 were subject to unsolicited takeovers. See Gerald F. Davis & Suzanne K. Stout, *Organization Theory and the Market for Corporate Control: A Dynamic Analysis of the Characteristics of Large Takeover Targets, 1980-90*, 37 ADMIN. SCI. Q. 605, 608 (1992).

90. Laurence Zuckerman, *Shades of the Go-Go 80's: Takeovers in a Comeback*, N.Y. TIMES, Nov. 3, 1994, at A1. The high yield or "junk" bond market expanded exponentially from \$7 billion in 1970 to \$146 billion in 1988, the increase due mainly to use of this financing in corporate control transactions. Charles M. Nathan & Eric A. Lopez Sr., *Hedge Funds and M&A—New Sharks and Too Little Shark Repellent*, in SECURITIES REGULATION IN EUROPE: A CONTRAST IN EU & US PROVISIONS 515, 521 (PLI Corp. Law and Practice, Course Handbook Series No. 6100, Dec. 2005).

91. For definitions of each of these, see generally Richard S. Ruback, *An Overview of Takeover Defenses*, in MERGERS & ACQUISITIONS 49 (Alan J. Auerbach ed., 1988).

92. One could literally write a book, and quite a juicy one at that, on this period or even its individual events. See, e.g., BRYAN BURROUGH & JOHN HELYAR, BARBARIANS AT THE GATE: THE FALL OF RJR NABISCO (2003) (chronicling the takeover battle for RJR Nabisco in 1988); ALLAN SLOAN, THREE PLUS ONE EQUALS BILLIONS: THE BENDIX-MARTIN MARIETTA WAR (1983) (chronicling the takeover battle between Bendix and Martin-Marietta in 1982). But I have selected for discussion in this Part three of the more telling examples during the period of SEC takeover regulation and activity.

1. SEC Legislative and Regulatory Efforts

The first of these efforts was the SEC's continued attempts to revise and expand the reach of the Williams Act. In 1983, the SEC formed an Advisory Committee on Tender Offers⁹³ (Advisory Committee) comprised of eighteen prominent members of the takeover community.⁹⁴ The Advisory Committee promptly reported fifty recommended revisions to federal takeover regulation in June of that year.⁹⁵ In March of 1984, the SEC Commissioners considered the recommendations; the SEC Commissioners rejected the sweeping ones, including a prohibition on charter and bylaw amendments which erected "high barriers to change of control."⁹⁶ Nonetheless, the SEC Commissioners did accept the majority of recommendations.⁹⁷ The rationale for the SEC Commissioners' rejection of a bar on takeover defenses particularly was never explained. However, the Delaware and other state courts had not yet ruled on the validity of these defenses, and the SEC's forbearance could be attributed to a wait-and-see approach with respect to this possible state action.⁹⁸ In May of that year, the SEC proposed implementing legislation for the accepted recommendations, including legislative curbs on greenmail and golden parachutes.⁹⁹

But events of the fourth wave soon forced the SEC to refocus its modest legislative agenda. By 1985, the rise of unsolicited takeovers in the public consciousness, and the negative public perceptions thereof, led to active congressional interest.¹⁰⁰ In that year alone, forty-one bills proposing to regulate take-

93. Advisory Committee on Tender Offers Establishment and Meeting, Exchange Act Release No. 19528, [1982-1983 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,319 (Feb. 24, 1983).

94. See generally SELIGMAN, *supra* note 16, at 584-85 (describing the history and composition of the committee).

95. SEC Advisory Committee on Tender Offers, Report of Recommendations and Commission Positions (July 8, 1983), *reprinted in* TENDER OFFERS 30-43 (Marc I. Steinberg ed., 1985) [hereinafter Advisory Committee Report].

96. See Statement of John S.R. Shad, Chairman of the Securities and Exchange Commission, Concerning the Recommendation of the SEC Advisory Committee on Tender Offers, [1983-1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,511, at 86,681 (Mar. 28, 1984) [hereinafter SEC Advisory Committee Response]. For example, the SEC stated that it had serious reservations concerning Recommendation 14, which would require any acquisition of more than twenty percent of the voting power of a corporation be acquired from the corporation itself or pursuant to a tender offer. *Id.* at 86,679-81.

97. The SEC Commissioners proposed legislation for five of the recommendations, agreed to support pending congressional legislation on golden parachutes, and ordered the SEC staff to take rulemaking action with respect to fourteen other recommendations. *Id.* at 86,684. See generally Linda C. Quinn & David B.H. Martin, Jr., *The SEC Advisory Committee on Tender Offers and Its Aftermath—A New Chapter in Change-of-Control Regulation*, in TENDER OFFERS, *supra* note 95, at 21-25 (outlining the SEC's response to the Advisory Committee Report).

98. The SEC Commissioners stated that they shared the "serious concerns" of the Advisory Committee but were "not prepared at this time to concur in such a broad intrusion into state corporate law." SEC Advisory Committee Response, *supra* note 96, at 86,681.

99. Tender Offer Reform Act of 1984, H.R. 5693, 98th Cong. (1984). The bill was submitted by the SEC to Congress on May 21, 1984, and introduced on May 22, 1984.

100. See, e.g., Peter Behr, *Inside the Economy*, WASH. POST, Jan. 5, 1984, at D9 (discussing increasing public concern over unsolicited takeovers and consequent proposals for regulation).

overs were introduced in Congress¹⁰¹—compared to one bill in 1980.¹⁰² These bills largely sought to tip takeover regulation in favor of targets by permitting takeover defenses and limiting bidder conduct.¹⁰³ The SEC opposed these bills. Instead, the SEC favored minority legislation preserving a level playing field and stockholder choice, increasingly calling for limits or even preemption of certain antitakeover measures such as the poison pill.¹⁰⁴ Even the SEC's own 1984 bill became caught in the storm; in 1985 it was amended into its opposite, an antitakeover law.¹⁰⁵ The SEC promptly committed filicide by issuing a public statement opposing these protarget amendments and killing its own proposed legislation.¹⁰⁶ In the end, the SEC's active energies would not produce passage of a takeover bill it favored, but, aided in large part by the Reagan Administration, the SEC would maintain the status quo and help defeat the proposed antitakeover legislation.¹⁰⁷

Legislative revision and initiative potential largely lost, the SEC attempted to respond and strengthen the Williams Act through regulatory action.¹⁰⁸ In 1986, in retort to a number of adverse court decisions, the SEC issued a concept release concerning the definitional scope of a tender offer, namely "whether the Williams Act should apply whenever a person acquires a substantial percentage of a target company's securities during or shortly after a tender offer."¹⁰⁹ The

101. Roberta Romano, *The Future of Hostile Takeovers: Legislation and Public Opinion*, 57 U. CIN. L. REV. 457, 470-71 (1988).

102. *Id.*

103. *See, e.g.*, S. 286, 99th Cong. (1985); S. 631, 99th Cong. (1985); S. 706, 99th Cong. (1985); S. 860, 99th Cong. (1985); S. 1882, 99th Cong. (1985); S. 1907, 99th Cong. (1985); H.R. 1480, 99th Cong. (1985); H.R. 5694, 98th Cong. (1984).

104. *See The Battle over Tender Offer Reform: From the States and the Courts to Congress*, 20 Sec. Reg. & L. Rep. (BNA) 60 (Jan. 15, 1988) (reviewing the SEC position during the period on proposed congressional tender offer legislation).

105. These amendments would have required a bidder to file a community impact statement, extended the minimum tender offer period to forty calendar days, and eliminated restrictions on management ability to take defensive action. *See Tender Offer Reform Act of 1984, supra* note 99.

106. *See SEC Says It Opposes House Measure to Restrict Abusive Takeover Tactics*, 16 Sec. Reg. & L. Rep. (BNA) 1473-74 (Sept. 14, 1984). The Reagan Administration also came out in strong opposition to the bill. *See Reagan Administration Formally Opposes House Bill to Limit Tender Offer Abuses*, 16 Sec. Reg. & Law Rep. (BNA) 1546 (Sept. 28, 1984). The Reagan Administration's position was distinct from the SEC's opposition. Secretary of the Treasury Donald Regan objected to the Bill on deregulatory and federalism bases writing that the Bill "intrude[s] unnecessarily into state law and constitute[s] an unwarranted step toward imposition of a substantive federal corporation law." *Id.*

107. *See* Subcomm. on Annual Review, *Annual Review of Federal Securities Regulation*, 40 BUS. LAW. 997, 1016-23 (1985) (outlining SEC and Reagan Administration opposition to proposed congressional takeover legislation). Congress did eventually act to inhibit the use of greenmail and golden parachutes by imposing excise taxes on their use. I.R.C. §§ 162(k), 280G (1988).

108. *See, e.g., Commission Will Not Reintroduce Takeover Legislation Package, Shad Says*, 17 Sec. Reg. & L. Rep. (BNA) 573 (Apr. 5, 1985). The only other major takeover reform bill of the decade reported out of congressional committee was the Tender Offer Reform Act of 1987; it restricted greenmail and golden parachutes and would have required stockholder approval of certain takeover defenses. Tender Offer Reform Act of 1987, H.R. 2172, 100th Cong. (1987). It, too, died in Congress.

109. Concept Release on Takeovers and Contests for Corporate Control: Advance Notice of Possible Commission Actions, Exchange Act Release No. 23486, [1986-1987 Transfer

next year the SEC proposed rules to regulate such purchases, but, as with other regulatory initiatives on this issue, these rules were never adopted.¹¹⁰ Interestingly, in the concept release, the SEC for the first time contemplated economic deregulation of tender offers, requesting for comment upon but never responding to the question of whether the Commission should adopt “a self-governance exemption to . . . provisions of its tender offer regulations.”¹¹¹

Meanwhile, the SEC was also using its regulatory powers to reconsider existing rules. In 1984, the SEC Commission, after considering deregulation of short tendering, decided to amend Rule 10b-4, over one dissent, to wholly ban hedged tendering.¹¹² In 1986, the SEC also amended the proxy disclosure rules to raise the disclosure obligations with respect to acquisition transactions.¹¹³ Finally and also in that year, the SEC amended the rules governing issuer tender offers to harmonize them with the third party tender offer rules and address certain controversial practices by targets in defensive buy-backs.¹¹⁴

2. *Antitakeover Measures*

The second mainstay SEC effort during this era was its increasing vocal and active opposition to the use of antitakeover measures. As the fourth wave progressed, states enacted antitakeover statutes and target corporations increasingly resorted to antitakeover defenses. In response, the SEC took a progressively more public position that corporate, judicial and legislative actions permitting or implementing antitakeover measures diminished stockholder choice and were therefore unacceptable.¹¹⁵

a. *Poison Pills*

The first prong of the SEC’s campaign was its active opposition to the adoption of antitakeover devices by corporations. The SEC initially raised this issue in 1979; the SEC stated publicly that it “[was] becoming increasingly concerned by the effect of defensive corporate charter amendments on the interests of in-

Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,018, at 88,199 (July 31, 1986) [hereinafter 1986 Concept Release].

110. Acquisitions of Substantial Amounts of Securities and Related Activities Undertaken During and Following a Tender Offer for Those Securities, Exchange Act Release No. 24976, [1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,160 (Oct. 1, 1987). These rules were likely not finalized due to widespread adoption of the poison pill and its inhibiting effect on these purchases, rendering the need for regulation largely unnecessary.

111. 1986 Concept Release, *supra* note 109, at 88,200.

112. Short Tendering Rule, Exchange Act Release No. 20799, [1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶83,601, at 86,712-13 (Mar. 29, 1984) [hereinafter Short Tendering Release]. For a definition of hedged tendering, see Robert F. Kramer, *Securities Exchange Act Rule 10b-4: The Second Circuit Considers Whether Short and Hedged Tendering Are Manipulative Devices*, 54 BROOK. L. REV. 649, 649 (1988).

113. Proxy Rules—Comprehensive Review, Exchange Act Release No. 22195, [1985-1986 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,901 (July 1, 1985).

114. Tender Offers by Issuers, Exchange Act Release 22788, [1985-1986 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,954 (Jan. 14, 1986).

115. See *infra* Part II.C.2.a.

vestors, particularly investors who are confronted with a tender offer.¹¹⁶ This concern transformed into active opposition as the decade progressed and their use became widespread. I have already noted the SEC's mid-1980s legislative proposals and support of congressional action to stem the use of greenmail and golden parachutes. But the SEC also pursued this cause through the regulatory process and the courts, particularly focusing on the *bête noire* of the age, the poison pill invented by Marty Lipton in 1982.¹¹⁷

The focus of the SEC's judicial strategy was primarily an argument to ban poison pills in Delaware state court in the 1985 case of *Moran v. Household Int'l, Inc.*¹¹⁸ The SEC effort, however, was unsuccessful, and the court in *Moran* validated use of the poison pill as a proportional target defensive response.¹¹⁹ Thereafter, the SEC unabashedly persisted in its campaign. In 1986, the SEC published a study of poison pills by its Chief Economist finding that "poison pills are harmful to target shareholders, on net [and there is] no statistical evidence that pills have systematically benefited target shareholders."¹²⁰ Thereafter, the SEC requested public comment on a rule which would have required stockholder preapproval of poison pills.¹²¹ The SEC abandoned this proposed rule shortly thereafter. The SEC's stated reason was that, due to substantial resolution of investor concerns surrounding these defenses by the state courts, regulation was not appropriate at the time.¹²²

116. 1979 Proposed Rules Release, *supra* note 77, at 82,614.

117. Lipton purportedly conceived of the poison pill to aid El Paso Railroad in fending off an unsolicited offer by Burlington & Northern Railroad. See Guhan Subramanian, *A New Takeover Defense Mechanism: Using an Equal Treatment Agreement as an Alternative to the Poison Pill*, 23 DEL. J. CORP. L. 375, 397 n.128 (1998). The SEC during this time period also attempted to prohibit dual-class voting stock which was claimed to unduly infringe upon the fundamental corporate concept of one-share-one-vote and preclude takeovers. The SEC responded in 1988 by promulgating Rule 19C-4, which prohibited publicly listed corporations from maintaining dual-class stock. This rule was invalidated by the D.C. Circuit on the grounds that it was beyond the SEC's rulemaking authority under section 19(c) of the Exchange Act. See *Bus. Roundtable v. SEC*, 905 F.2d 406, 407 (D.C. Cir. 1990). See generally Stephen M. Bainbridge, *The Short Life and Resurrection of SEC Rule 19C-4*, 69 WASH. U. L.Q. 565 (1991).

118. 500 A.2d 1346 (Del. 1985). The SEC filed an amicus brief in *Moran. Id.* at 1348. The SEC's decision to intervene was made on a three to two vote by the SEC Commissioners. *Id.* at 1348 n.1. The SEC argued that a "[b]oard is unauthorized to usurp stockholders' rights to receive hostile tender offers" and "unauthorized to fundamentally restrict stockholders' rights to conduct a proxy contest." *Id.* at 1351. See generally Martin M. Cohen, Note, "Poison Pills" as a Negotiating Tool: Seeking a Cease-Fire in the Corporate Takeover Wars, 1987 COLUM. BUS. L. REV. 459, 471-77 (1987) (discussing the SEC's intervention in *Moran*).

119. *Moran*, 500 A.2d at 1353-56.

120. OFFICE OF THE CHIEF ECONOMIST, SEC, THE EFFECTS OF POISON PILLS ON THE WEALTH OF TARGET SHAREHOLDERS 43 (1986). These results were consistent with an earlier study by the SEC Chief Economist. See *A Study on the Economics of Poison Pills [1985-1986 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,971*, at 88,044 (Mar. 5, 1986) (concluding that the "effect[s] of poison pills [in deterring] prospective hostile takeover bids out-weighs the beneficial effects that come from increased bargaining leverage of the target management").

121. 1986 Concept Release, *supra* note 109, at 88,206.

122. See *Tender Offer Reform, Hearing Before the Subcomm. on Telecommunications and Finance of the H. Comm. on Energy and Commerce*, 100th Cong. (1987) (statement of

Here, the SEC was likely referring not to *Moran* but to two revolutionary Delaware Court decisions. In 1985, the Delaware Supreme Court decided *Unocal Corp. v. Mesa Petroleum Co.*¹²³ and *Revlon, Inc. v. MacAndrews & Forbes Holdings*.¹²⁴ *Unocal* and *Revlon* were uniquely consequential for holding that the takeover decision and the use of takeover defenses would now be reviewed by the Delaware courts under a higher standard than the business judgment rule.¹²⁵ Though these decisions left undefined the initial parameters of this review and its limitations, they initially appeared to circumscribe the use of takeover defenses—hence, the SEC’s forbearance. For the remainder of the 1980s, the Delaware courts would be an active regulator of takeovers through exposition and application of these two decisions and their required standards of review.¹²⁶

b. State Takeover Legislation

The second prong of the SEC offense was its consistent opposition to state takeover legislation. In the mid-1970s, the states began to stir and legislate their own takeover laws.¹²⁷ These first generation statutes were almost all patterned upon blue sky laws and went beyond the Williams Act. In their most common form, these laws subjected a takeover offer to a precommencement waiting pe-

David S. Ruder, Chairman, Securities and Exchange Commission). The SEC action was also likely causally related to congressional and even administration opposition to such a proposal. For example, the Reagan Administration’s Economic Policy Council came out forcefully during this time period against congressional action to prohibit takeover defenses. Administration Group Rejects Proposal to Enter Debate on Corporate Takeovers, 19 Sec. Reg. & L. Rep. (BNA) 819 (June 5, 1987).

123. 493 A.2d 946 (Del. 1985). In *Unocal*, the Delaware Supreme Court held that a target board decision to take defensive action in light of a threat to the corporation—in this case an unsolicited two-tiered takeover offer combined with the threat of greenmail—should not be reviewed under the business judgment rule but rather a higher, intermediate standard. *Id.* at 955. See generally Ronald J. Gilson & Reinier Kraakman, *Delaware’s Intermediate Standard for Defensive Tactics: Is There Substance to Proportionality Review?*, 44 BUS. LAW. 247 (1989) (reviewing the *Unocal* decision and Delaware courts’ subsequent interpretation thereof).

124. 506 A.2d 173 (Del. 1986). The *Revlon* case is discussed further at *infra* Part IV.A.

125. See Sean J. Griffith, *Good Faith Business Judgment: A Theory of Rhetoric in Corporate Law Jurisprudence*, 55 DUKE L.J. 1, 61-63 (2005) (stating that “the creation of *Revlon* duties shifted the frontier of the authority/accountability spectrum in favor of greater board accountability to courts”); Robert A. Prentice & John H. Langmore, *Hostile Tender Offers and the “Nancy Reagan Defense”: May Target Boards “Just Say No”? Should They Be Allowed To?*, 15 DEL. J. CORP. L. 377, 383-85 (1990) (discussing *Revlon*’s and *Unocal*’s raised standards of review with respect to takeover defenses).

126. For example, in the 1980s, the Delaware Court of Chancery held in six cases that a board’s responsive action in the face of a takeover bid was disproportionate under *Unocal*. See *Grand Metro. Pub. Ltd. v. Pillsbury Co.*, 558 A.2d 1049 (Del. Ch. 1988); *City Capital Assocs. v. Interco Inc.*, 551 A.2d 787 (Del. Ch. 1988); *Robert M. Bass Group, Inc. v. Evans*, 552 A.2d 1227 (Del. Ch. 1988); *Tate & Lyle PLC v. Staley Cont’l, Inc.*, Civ. A. No. 9813, 1988 WL 46064 (Del. Ch. May 9, 1988); *I.P. Phillips v. Insituform of N. Am., Inc.*, Civ. A. No. 9173, 1987 WL 16285 (Del. Ch. Aug. 27, 1987); *AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103 (Del. Ch. 1986).

127. See generally Diane S. Wilner & Craig A. Landy, *The Tender Trap: State Takeover Statutes and Their Constitutionality*, 45 FORDHAM L. REV. 1, 3 (1976) (observing in 1976 that twenty-three states had recently enacted takeover statutes). Delaware enacted a first generation statute on May 1, 1976. DEL. CODE ANN. tit. 8, § 203(c)(2) (1977).

riod and approval by a state administrator.¹²⁸ I have already noted that the SEC had acted in 1979 to preempt a number of these statutes.¹²⁹ But, as the fourth wave gathered steam, the number of state legislatures adopting takeover statutes increased in response to heightened public hostility to takeovers mixed with opportune corporate lobbying.¹³⁰ The SEC vocally and continually opposed this legislation as against its level-playing-field policy as well as on the grounds that these laws were either preempted or an unconstitutional burden on interstate commerce.¹³¹

In the Supreme Court case *Edgar v. MITE Corp.*,¹³² the SEC succeeded: Illinois' first generation takeover statute was struck down as unconstitutional.¹³³ However, the states quickly counterattacked, enacting modified and more limited second generation takeover statutes.¹³⁴ The content of these statutes was less far-reaching than first generation laws; they purported to regulate corporate internal affairs, such as stockholder or board approval procedures, rather than the exogenous matter of the takeover process.¹³⁵ In *CTS Corp. v. Dynamics Corp. of America*,¹³⁶ the Supreme Court set back this SEC effort by holding Indiana's second generation law to be constitutional.¹³⁷ Within six months of

128. See generally Donald C. Langevoort, *State Tender-Offer Legislation: Interests, Effects, and Political Competency*, 62 CORNELL L. REV. 213, 219-33 (1977) (describing first generation takeover laws).

129. See *supra* notes 86-87 and accompanying text.

130. By 1982, thirty-seven states had adopted a form of takeover statute. These statutes are listed in Mark A. Sargent, *On the Validity of State Takeover Regulation: State Responses to MITE and Kidwell*, 42 OHIO ST. L.J. 689, 690 n.7 (1981).

131. The SEC had consistently opposed this regulation since its first appearance in the 1970s. See Wilner & Landy, *supra* note 127 (reviewing early state takeover statutes and arguments that they "frustrated" the purposes of the Williams Act and "unconstitutionally" burdened interstate commerce).

132. 457 U.S. 624 (1982).

133. *Id.* at 646. The SEC filed an amicus brief in *MITE* asserting that the statute was constitutionally infirm because it alternatively violated the commerce clause or was preempted by the Williams Act. Brief for the Securities and Exchange Commission as Amicus Curiae Supporting Petitioner, *Edgar v. MITE Corp.*, 457 U.S. 624 (1982) (No. 80-1188), 1981 WL 389721.

134. In the six-year period after *MITE*, twenty states enacted takeover statutes. Romano, *supra* note 101, at 461. See also Allen D. Boyer, *Federalism and Corporation Law: Drawing the Line in State Takeover Regulation*, 47 OHIO ST. L.J. 1037, 1062-65 (1986) (tracing state reactions to the decision in *MITE* and their passage of second generation takeover laws).

135. Second generation statutes had a more confined jurisdictional scope: they limited their application to corporations organized within the state. In addition, they almost always had opt-out or opt-in provisions which permitted corporate choice as to whether to apply the statute. See generally Roberta Romano, *The Political Economy of Takeover Statutes*, 73 VA. L. REV. 111, 113-17 (1987) (describing the types of takeover statute and setting forth states adopting them).

136. 481 U.S. 69 (1987).

137. *Id.* at 94. The SEC also filed an amicus brief in *CTS Corp.* In contrast to its amicus brief in *MITE*, the SEC argued that the statute was constitutionally invalid under the commerce clause but did not reargue invalidity under preemption doctrine. Brief for the Securities and Exchange Commission and the United States as Amici Curiae Supporting Respondents, *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69 (1987) (Nos. 86-71 & 86-97), 1987 WL 880969.

CTS, fifteen states proceeded to enact some species of these laws.¹³⁸ Importantly, the post-CTS wave included a second generation law enacted by Delaware which, over SEC public objection, passed a business combination statute modeled on New York's.¹³⁹

Nonetheless, the SEC continued its aggressive prosecution of its unconstitutionality claims *vis-à-vis* these new second generation laws. The SEC attitude during this time was summed up by the SEC General Counsel Daniel Goelzer, who stated in 1988,

[T]he [C]ommission has instructed us to support challenges to the constitutionality of the Delaware [antitakeover] statute . . . I identified that as a top priority because our success or failure in those challenges will have a far[-]reaching effect on tender offer practice and quite likely on what Congress does with respect to tender offer legislation.¹⁴⁰

In line with this testimony, the SEC actively argued in amicus filings in state courts to declare state takeover statutes unconstitutional, including the Delaware law referred to in the quote above. These efforts were wholly unsuccessful.¹⁴¹ The SEC Chairman at the time, David S. Ruder, also went before Congress and futilely attempted to prod it into passing legislation providing the SEC with authority to preempt state takeover laws.¹⁴² While the SEC ultimately failed in its endeavor to restrict takeover defenses and preempt state takeover statutes, it could not be denied that the SEC had unreservedly made an attempt and, at least partially, succeeded in limiting the effects and scope of state takeover statutes.¹⁴³

138. David F. Crabtree, Note, *The Constitutionality of State Takeover Legislation Revisited: The Effect of CTS Corp. v. Dynamics Corp. of America*, 1988 UTAH L. REV. 675, 679 n.23 (1988).

139. The Delaware law was a relatively modest version of takeover law, a fact possibly attributable to vocal SEC lobbying against Delaware's adoption of any takeover statute. See Romano, *supra* note 101, at 463-65.

140. *Major Change in Direction Under Debate in SEC Bankruptcy Program*, Goelzer Says, 20 Sec. Reg. & L. Rep. (BNA) 1171, 1176 (July 22, 1988). The SEC campaign generally extended against all species of takeover statute. See, e.g., Joseph Grundfest, Letter to the Honorable Mario M. Cuomo, reprinted in GILSON & BLACK, *supra* note 22, at 1392-93 (letter from the SEC Commissioner to the Governor of New York arguing against the adoption by New York state of an antitakeover constituency statute).

141. For example, the SEC subsequently filed amicus briefs in three federal district court cases arguing that the takeover statutes before the court in each instance were unconstitutional on commerce clause and preemption grounds. See *RP Acquisition Corp. v. Staley Continental, Inc.*, 686 F. Supp. 476 (D. Del. 1988); *Salant Acquisition Corp. v. Manhattan Indus.*, 682 F. Supp. 199 (S.D.N.Y. 1988); *RTE Corp. v. Mark IV Industries*, 1988 WL 75453 (E.D. Wis. May 6, 1988). See also Johnson & Millon, *supra* note 40, at 1882-86 (discussing the SEC amicus curiae briefs in these cases).

142. The SEC's position was largely opposed by other members of the Reagan administration. See Witnesses at Takeover Bill Hearing Split on Preemption of State Regulation, 19 Sec. Reg. & L. Rep. (BNA) 851 (June 12, 1987).

143. This failure with respect to takeover defenses, however, was complete. By the end of the 1980s, almost every publicly traded corporation had adopted one or more antitakeover devices. See INVESTOR RESP. RES. CTR. INC., CORPORATE TAKEOVER DEFENSES 1989 (Virginia K. Rosenbaum ed., 1989).

3. *Specific SEC Action*

The third of the SEC's efforts consisted of actions to address two of the more prevalent and problematic takeover tactics in the fourth wave—the two-tiered tender offer¹⁴⁴ and the exclusionary self-tender.¹⁴⁵ As the fourth wave continued, the SEC acted with respect to the two-tiered offer: on December 15, 1982, the SEC revised Rule 14d-8 to extend the minimum proration period for partial tender offers to twenty business days.¹⁴⁶ This SEC action was again an aggressive one, illustrated by the dissent of the SEC Chairman and another commissioner who argued that the new rules were *ultra vires* since they conflicted with the plain language of section 14(d)(6) of the Securities Exchange Act of 1934, as amended (Exchange Act).¹⁴⁷ The SEC subsequently and repeatedly acted to place the issue of two-tiered offers in the public realm by issuing a notice of possible commission action¹⁴⁸ and then releasing a study by the Chief Economist of the SEC finding that two-tiered offers largely had no adverse effects.¹⁴⁹ Ultimately, however, the SEC never attempted to further regulate two-

144. In its most common form, the front-loaded, two-tiered tender offer involved two steps. First, the bidder would initiate a tender offer to acquire a controlling interest in the target. The consideration in this first step would typically be cash. Thereafter, in the second step the bidder would "freeze-out" the minority interest and acquire the remaining target shares through a compulsory acquisition process. In this second step, the consideration would sometimes be securities with a lower value than the initial cash consideration offered. See generally Comment, *Front-End Loaded Tender Offers: The Application of Federal and State Law to an Innovative Corporate Acquisition Technique*, 131 U. PA. L. REV. 389, 390-94 (1982) (describing a typical two-tiered offer in the context of the competitive bidding by U.S. Steel and Mobil for Marathon Oil). The coercive element is self-evident: in the absence of takeover defenses, stockholders are incentivized to tender into the offer so as to ensure receipt of the certain value of the cash consideration. See generally Lucian Arye Bebchuk, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 HARV. L. REV. 1693, 1717-35 (1985) (describing the coercive nature of two-tiered tender offers).

145. The exclusionary self-tender is a defensive tactic: the target launches a self-tender offer for its shares at a price that is a premium to market but which, by its terms, prohibits the hostile bidder from tendering into this offer. An exclusionary self-tender can be particularly effective in the face of a front-loaded, two-tiered tender offer because it provides an alternative to target stockholders and ostensibly compensates these stockholders for a lower back-end in the bidder's offer. See Kenneth B. Pollock, Note, *Exclusionary Tender Offers: A Reasonably Formulated Takeover Defense or a Discriminatory Attempt to Retain Control?*, 20 GA. L. REV. 627, 633-41 (1986) (describing the use of an exclusionary self-tender offer by Unocal in the face of an unsolicited offer by Mesa Petroleum).

146. Pro Rata Rule, Exchange Act Release No. 19336, [1982-1983 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,306 (Dec. 15, 1982).

147. *Id.* at 85,652 (dissent of SEC Commissioner John Shad). See also W. Brewster Lee, III, Note, *SEC Tender Offer Timing Rules: Upsetting a Congressionally Selected Balance*, 68 CORNELL L. REV. 914 (1983) (arguing that the SEC promulgation of Rule 14d-8 was beyond the scope of its statutory rulemaking authority).

148. See Two-Tier Tender Offer Pricing and Non-Tender Offer Purchase Programs—Advance Notice of Possible Commission Action, Exchange Act Release No. 21079, [1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,637 (June 21, 1984).

149. OFFICE OF THE CHIEF ECONOMIST, SEC, *THE ECONOMICS OF ANY-OR-ALL, PARTIAL, AND TWO-TIER TENDER OFFERS* (1985).

tiered offers, as the rise of the poison pill anesthetized their coercive element and constrained their use by bidders.¹⁵⁰

In contrast, the SEC acted definitively with respect to the exclusionary self-tender. When the Delaware Supreme Court in *Unocal* upheld an exclusionary self-tender in the face of an unsolicited bid for Unocal Corp. by the well-known corporate raider T. Boone Pickens, the SEC took direct action on the all-holders rule it had previously contemplated in 1979. In 1986, the SEC amended Rules 14d-10 and 13e-4 to include an all-holders rule and a revised best-price rule.¹⁵¹ The new all-holders rule was specifically enacted to overturn the Delaware ruling by prohibiting exclusionary issuer and third party tender offers of any nature.¹⁵² Notably, this release also amended Rule 14d-7 to provide for withdrawal rights throughout the entire tender offer period.¹⁵³

D. Federal Takeover Regulation Circa 1989

Things were different as the sun set on the 1980s. The regulation of takeovers in the 1960s had been the SEC's untrammelled domain. In 1968, the year of the Williams Act, Virginia was the only state with a takeover statute.¹⁵⁴ Additionally, state courts at that time only sporadically addressed takeover issues and treated them largely as if they were any other general corporate matter, typically applying the business judgment rule and its "hands off" imprimatur to scrutinize these takeover-related decisions.¹⁵⁵ But by the close of the 1980s, takeover regulation in the United States was a duopoly of the states and the SEC. Interestingly, the state component was now principally the state courts rather than the legislatures. Although second and later generation takeover statutes had been enacted by the state legislatures,¹⁵⁶ the substantive regulation and

150. See Coates, *supra* note 8, at 321.

151. Amendments to Tender Offer Rules—All-Holders and Best-Price, Exchange Act Release No. 23421, [1986-1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,016 (July 11, 1986) [hereinafter All-Holders Release].

152. Proposed Amendments to Tender Offer Rules, Exchange Act Release No. 22198, [1984-1985 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,797, at 87,560 (July 1, 1985). The all-holders rule was controversial and once again viewed by some commentators as beyond the SEC's rulemaking authority. All-Holders Release, *supra* note 151, at 88,188-91. See generally Roberta S. Karmel, *Authority for the Tender Offer Rules*, 216 N.Y. L.J. 3 (Dec. 19, 1996) (noting SEC authority to promulgate Rules 14d-10 and 13e-4 was sternly questioned during the rulemaking process).

153. All-Holders Release, *supra* note 151, at 88,196-97. The SEC also amended Rules 13e-4(f)(1)(ii) and 14e-1(b) to require that the tender offer period remain open for ten business days after the announcement of an increase or decrease in the percentage of securities being sought or in the consideration offered. *Id.* at 88,195-96.

154. The Virginia takeover statute was enacted shortly before the passage of the Williams Act on March 5, 1968. See Martin Lipton & Paul K. Rowe, *Pills, Polls and Professors: A Reply to Professor Gilson*, 27 DEL. J. CORP. L. 1, 4 n.11 (2002).

155. See generally Edward F. Greene & James J. Junewicz, *A Reappraisal of Current Regulation of Mergers and Acquisitions*, 132 U. PA. L. REV. 647, 711 (1984) (stating that "[s]tate regulation, however, is not likely to be effective [to regulate takeovers] because the business judgment rule is the method used to review those corporate actions").

156. See Arthur R. Pinto, *The Constitution and the Market for Corporate Control: State Takeover Statutes After CTS Corp.*, 29 WM. & MARY L. REV. 699, 713-16 (1988) (discussing the states' adoption of takeover statutes post-*CTS Corp.*).

state administrative oversight embedded in first generation takeover statutes had been left by the wayside. These new statutes merely set forth procedural anti-takeover strictures to be adhered to by the takeover participants and enforced by the state courts.¹⁵⁷ The state courts, by weaving a web of heightened takeover standards, went much further—placing themselves in a permanent supervisory position over takeovers.¹⁵⁸ Accordingly, by the end of the 1980s, takeover regulation was largely the province of the SEC and the state courts, principally Delaware.¹⁵⁹

This overlapping jurisdiction and regulation created an uneasy marriage. In broad terms, the SEC regulation primarily controlled disclosure and the substantive and procedural aspects of the tender offer process itself. Meanwhile, state law promulgated by the courts controlled the corporate decision-making process: the so-called internal affairs doctrine.¹⁶⁰ But, as discussed above, there was much conflict and overlap among the two. For example, both the SEC and state courts actively sought to regulate or considered regulation of takeover defenses, going-privates and exclusionary self-tenders.¹⁶¹ Meanwhile, the interweave of state and federal regulation of proxy contests foreclosed categorization between the two.¹⁶² In short, while the regulatory focus was divergent, there was no clear demarcation of role between the two actors, and, if anything, the federal component was dominant.¹⁶³ In light of this overlap, the 1980s finished with both the SEC and state courts actively competing to regulate almost every aspect of the takeover.

157. *See id.*

158. *See supra* Part II.C.2.

159. *Cf.* Lyman Johnson, *The Delaware Judiciary and the Meaning of Corporate Life and Corporate Law*, 68 TEX. L. REV. 865, 872-73 (1990) (“Therefore, not only has the task of speaking to the takeover phenomenon centered on state rather than federal forums, the true locus of power has shifted from the legislative branch to the Delaware judiciary.”).

160. The internal affairs doctrine is a conflict of laws principle that leaves matters of internal corporate governance to be regulated by the state that charters the corporation. In the realm of takeovers, the application of the principle has always been on shaky doctrinal ground. Where internal affairs (to be regulated by the chartering state) and third party, extra-corporate affairs (to be regulated by other states and possibly the federal government) begin and end is murky. *See, e.g.*, Jed Rubinfeld, *State Takeover Legislation and the Commerce Clause: The “Foreign” Corporations Problem*, 36 CLEV. ST. L. REV. 355, 379-80 (1988). The Supreme Court itself noted this problem in *MITE*, stating that “[the internal affairs] doctrine is of little use . . . in this context. Tender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company.” *Edgar v. MITE Corp.*, 457 U.S. 624, 645 (1982).

161. *See supra* Parts II.B & II.C.

162. State and federal law, as well as stock exchange rules, have historically combined without distinction to control both the substantive and procedural aspects of proxy contests. *See generally* RANDALL S. THOMAS ET AL., ARANOW & EINHORN ON PROXY CONTESTS FOR CORPORATE CONTROL (3d ed. 1998).

163. *See* Richard W. Painter, *Responding to a False Alarm: Federal Preemption of State Securities Fraud Causes of Action*, 84 CORNELL L. REV. 1, 15 (1999) (“Congress’s regulation of tender offers under the Williams Act represents the closest that it has come to encroaching on substantive corporate law”); Robert B. Thompson, *Preemption and Federalism in Corporate Governance: Protecting Shareholder Rights to Vote, Sell, and Sue*, 62 L. & CONTEMP. PROBS. 215, 242 (1999) (“The relationship between shareholders and directors within a corporation, long thought to be within the domain of state law, now has a dominant federal aspect.”).

Moreover, the revolution in bidder and target tactics and accompanying market developments transformed the takeover. The takeover of the 1980s was a very different animal than that of the 1960s. Two-tiered and partial offers using differing mixes of securities and cash were common, in contrast to the almost uniform use of the cash tender offer in the 1960s. Unsolicited offers and leveraged structures utilizing high-yield financing also became prevalent. The big difference, however, was that targets could now respond with defensive measures and thereby inhibit, if not preclude, an unsolicited takeover.¹⁶⁴ This was true despite the fact that targets were now subject to review under higher state court standards, leading many an unsolicited takeover to be decided in the courts.¹⁶⁵ This state court review, which typically validated target defensive action, placed the state courts in the role of umpire in the takeover game and effectively further slowed the pace of takeovers.¹⁶⁶

Meanwhile, on the federal level, the SEC had erected a scaffold of rules generally applicable to takeover transactions and special regulation applicable to issuer tender offers and going-private transactions. These rules largely followed the long-held SEC positions of neutrality *vis-à-vis* targets and bidders and protection of the common stockholder.¹⁶⁷ However, other congressional legislation in the 1970s was not so neutral in its effect. The Hart-Scott-Rodino Antitrust Improvements Act of 1976 enacted an antitrust waiting and review period for acquisition transactions, including tender offers.¹⁶⁸ The 1988 Exon-Florio Amendment to the Defense Production Act of 1950 also established a timeline for review of acquisition transactions affecting national security.¹⁶⁹ The result was to put a federal brake on the ability of many a bidder to swiftly consummate a tender offer or otherwise take preliminary acquisition measures.

Finally, the Williams Act marked the first and last coordinated piece of system-wide federal takeover regulation. Thereafter, the SEC promulgated takeover regulation largely in response to issues as they arose. The SEC did not, in this process, develop a principle-based approach to regulation—adopting general guidelines applicable to differing paradigms and unforeseen developments. Rather, the SEC issued regulation on a case-by-case basis keyed to specific

164. This was primarily due to the availability of the poison pill. See, e.g., Guhan Subramanian, *Fixing Freezeouts*, 115 YALE L.J. 2, 49 (2005) (“However, in practice, the poison pill makes board approval a prerequisite even for tender offers.”).

165. Professor David Skeel has noted that Delaware, in its quest to maintain its role as the epicenter of takeover regulation, has “taken numerous steps” to encourage such litigation to be sited in Delaware. See David A. Skeel, Jr., *The Unanimity Norm in Delaware Corporate Law*, 83 VA. L. REV. 127, 160 (1997).

166. See generally Peter J. Henning, *Corporate Law After the Eighties: Reflections on the Relationship Between Management, Shareholders and Stakeholders*, 36 ST. LOUIS U. L.J. 519, 613 (1992).

167. The SEC has generally observed neutrality in this regard, but as Professor Donald Langevoort has observed, the SEC has above all favored the average stockholder in its takeover regulation, introducing a “primary objective of egalitarianism.” Donald C. Langevoort, *The SEC as a Bureaucracy: Public Choice, Institutional Rhetoric, and the Process of Policy Formulation*, 47 WASH. & LEE L. REV. 527, 535 (1990).

168. Pub. L. No. 94-435, 90 Stat. 1390 (1976).

169. Pub. L. No. 100-418, 102 Stat. 1107, 1425, et seq. (1988).

problems.¹⁷⁰ The federal takeover code was thus one cobbled together from various pieces.

The one constant through all of this was the SEC. During this period, the SEC sometimes appeared schizophrenic in its regulatory goals and pronouncements.¹⁷¹ The SEC also often failed to implement its legislative, regulatory, and enforcement agenda. This is certain. But it is also clear that during this period the SEC, although not omnipotent, was a principal, if not the primary, regulator of takeovers.

III. THE WITHERING OF FEDERAL TAKEOVER REGULATION

The dual SEC/state court arrangement that existed at the end of the 1980s unexpectedly ended in the 1990s. The SEC largely abdicated its prior active role in takeover regulation outlined in Part II. This silence has been extended and significant. From 1989-2006, the SEC would only twice adopt new domestic takeover rules.¹⁷² This compares to the SEC's extensive domestic takeover-related rulemaking during the period 1969-1989.¹⁷³ Other hallmarks of SEC activity also evaporated; no longer did the SEC seek to publicly comment on the takeover issues of the day or otherwise strive to set takeover policy by proposing takeover legislation and rules, initiating fact-finding investigations, issuing concept releases, and conducting empirical and other research. In short, at the decade's turn, the SEC vanished from its role as an activist takeover regulator; it became seemingly content to administer the current regulatory apparatus.¹⁷⁴

But in fairness, the SEC's main foray into rulemaking during this period was substantial. In October 1999 the SEC in the M&A Release promulgated wholesale revisions to the tender offer, proxy, and other merger and acquisition-related rules.¹⁷⁵ The M&A Release had the stated goal of raising the federal takeover into the modern age, and it comprehensively revised the communication requirements for acquisition transactions, attempted to put stock and cash tender offers on equal parity, eliminated the five business day commencement

170. See generally J. Robert Brown, Jr., *Regulatory Intervention in the Market for Corporate Control*, 23 U.C. DAVIS L. REV. 1, 3 (1989) (stating that "[w]ith no central vision of an appropriate regulatory scheme, [SEC takeover rules] often emerge in an effort to ameliorate a specific abuse or to provide shareholders with some added benefit").

171. Two telling examples are, first, the SEC's desultory contemplation of, attempts to promulgate, and ultimate rejection of a rule to define "tender offers" to include unconventional purchases, and, second, the SEC's shifting position, contemplated rulemaking, and legislative proposals concerning takeover defenses, particularly with respect to the poison pill. See *supra* Parts II.B & II.C.

172. These were the rules promulgated and amended in the M&A Release discussed *infra* at notes 175-77 and accompanying text and the amendment to the all-holders/best price rule discussed *infra* at note 287. The SEC also adopted comprehensive regulation for cross-border acquisitions. See generally Brett A. Carron & Steven M. Davidoff, *Getting U.S. Security Holders to the Party: The SEC's Cross-Border Release Five Years On*, 26 U. PA. J. INT'L ECON. L. 455 (2005) (describing and analyzing the SEC's cross-border rules promulgated in 1999).

173. See *supra* Part II.

174. This observation has also been made by Professor Roe in his article *Delaware's Competition*. Roe, *supra* note 2, at 630.

175. M&A Release, *supra* note 51.

rule for tender offers, and simplified and revised acquisition disclosure requirements.¹⁷⁶ Although this regulatory action was undeniably important, it was designed to refine the SEC's own existing Exchange Act disclosure rules and update them for the technological age.¹⁷⁷ The action was also within SEC and not state domain, did not break any new ground, and did not address the significant takeover issues of the day or update the federal takeover code to comport with the new playing field created by the third and fourth waves.

It also did not take into account the issues of the latest wave. The fifth wave started in the mid-1990s, and it still runs fast today. The fifth wave peaked initially in the technology bubble with over \$1.7 trillion dollars in announced, domestic merger activity in 2000, paused slightly in 2001-2003 with the popping of that bubble and the events of September 11, but continues today with \$1.6 trillion in completed domestic takeover activity in 2006.¹⁷⁸ This wave, as with the third and fourth waves, engendered a transformation in deal structure and tactics. The majority of deals in the wave's first part, that is, until 2001, comprised stock rather than cash consideration and were structured as mergers rather than tender offers.¹⁷⁹ And leveraged structures using high-yield financing were much less frequent. However, in the second part of the fifth wave, that is, after 2003, leveraged structures and all cash transactions have again become more common due to the emergence of private equity as a dominant force in takeovers.¹⁸⁰ And throughout the entire wave, negotiated transactions became the norm and unsolicited or hostile offers, although still occurring, were less common than in the previous third and fourth waves.¹⁸¹

176. *Id.* at 82,578-80.

177. *Id.* at 82,579 (stating that “[w]e believe these new rules and revisions should provide participants in the securities markets sufficient flexibility to accommodate changes in deal structure and advances in technology that continue to occur”).

178. Thomson Financial, Fourth Quarter 2006 Mergers & Acquisitions Review available at http://www.thomson.com/pdf/financial/league_table/ma/150587/4Q06_MA_Global_Finl_Advisory (last visited on June 6, 2007) [hereinafter Thomson Financial].

179. A significant factor in the use of stock consideration during this time period was the inflated stock prices of corporations, particularly those in the technology sector, and the low relative cash-on-hand of these corporations illustrated by the all-time general low of dividend/price ratios. Not surprisingly, postboom there has been an observed proportional increase in cash deals. It is generally believed that this is also due to a trend towards more analytical and careful acquisition practices rather than other extrinsic factors such as the SEC's elimination of pooling accounting. See Joseph H. Flom, *Mergers and Acquisitions: The Decade in Review*, 54 U. MIAMI L. REV. 753, 769-70 (2000). Nonetheless, some have predicted that the elimination of pooling accounting has spurred the increased use of combination cash and stock consideration. *Id.*

180. The ability to use high-yield bonds to finance takeovers was limited to some extent in the 1980s by a 1986 Federal Reserve Board Ruling which restricted the utility of controlled-shell corporations. See INV. RESP. RES. CTR. STUDY, JUNK BONDS AND TENDER OFFER FINANCING (1986). But leveraged structures have become commonplace again in the prior two to three years due to the private equity boom. In 2006, private equity leveraged buy-outs comprised approximately twenty-six and a half percent of the domestic takeover market. Thomson Financial, *supra* note 178.

181. GAUGHAN, *supra* note 22, at 50-53. According to one study, 4% percent of transactions in the 1990s were unsolicited, compared to 14.3% and 8.4% percent in the 1980s and 1970s respectively. Gregor Andrade et al., *New Evidence and Perspectives on Mergers*, 15 J. ECON. PERSP. 103, 106 tbl.1 (2001).

The issues of both the third and the fourth waves, particularly those surrounding takeover defenses, going-privates, and applicable standards of review for takeover-related decisions, continued to percolate in the fifth one.¹⁸² But the fifth wave created its own unique issues. An issue at the forefront was parity between mergers and tender offers. The tendency of acquirers in the fifth wave to prefer mergers over tender offers was reinforced by internal biases in federal securities regulation, which often led acquirers to favor a merger structure. This is not to say that both these rules and state court regulation did not sometimes discriminate against mergers to the benefit of tender offers, for they did that too—just that the regulatory balance tilted in favor of mergers.¹⁸³ Another emergent issue was that of lock-ups:¹⁸⁴ the rise in negotiated transactions led to repeated disputes surrounding transaction defenses in the form of lock-ups and claims that they forced board negotiated transactions onto stockholders. Alternatives were foreclosed or inhibited.¹⁸⁵ Finally, the prevalence of leveraged private equity buy-outs and the tendency of these firms to partner with management to opportunistically time and advantage their acquisitions has reawakened concerns over going-privates. Yet the SEC slumbered on these fifth wave troubles as well as the old third and fourth wave ones; the SEC either did not even attempt to address them or took only limited action with respect thereto through the M&A Release.

Why did this happen? The SEC never provided an explanation. However, it can be surmised that it was in part due to the change in Presidential administrations. The first Bush Administration, unlike the Reagan one, did not express any particular interest in takeover regulation, and perhaps this was reflected in the SEC's dormancy.¹⁸⁶ In addition, the SEC Commissioners largely turned over at the time of the Bush Administration, and the new SEC Commissioners, in light of the issues raised by the crash of 1987, may not have been as concerned with takeovers as previous ones.¹⁸⁷ This thesis finds support in the continuing inaction through the Clinton and second Bush Administrations. Perhaps it was a

182. See *infra* Part IV (discussing the Delaware court's continuing treatment of these issues).

183. For a further discussion of tender offer biases under the federal securities law, see *infra* Part V.B.2.

184. A "lock-up" in the takeover context can be defined as a transaction defense mechanism whereby an acquiree agrees to compensate an acquirer upon the nonconsumation or breach of an acquisition agreement. Marcel Kahan & Michael Klausner, *Lockups and the Market for Corporate Control*, 48 STAN. L. REV. 1539, 1540 (1996). "Lock-ups" include break-up fees, termination fees, and stock and asset options. *Id.* The term also includes stockholder lock-ups—that is, agreements by stockholders to vote for or tender their shares in a takeover transaction.

185. See *infra* note 217 and accompanying text.

186. The most prominent takeover regulatory act by the Bush administration was the order issued to China National Aero-Technology Import and Export Corporation to divest its recently acquired holding in MAMCO Manufacturing, Inc. The Bush Administration issued this directive under the Exon-Florio Amendments after a finding that the acquisition was a threat to national security. See generally Christopher R. Fenton, Note, *U.S. Policy Towards Foreign Direct Investment Post-September 11: Exon-Florio in the Age of Transnational Security*, 41 COLUM. J. TRANSNAT'L L. 195, 209-11 (2002) (reviewing this Bush Administration action).

187. See also Roe, *supra* note 2, at 630.

product of the Reagan Administration's antiregulatory bent; the active SEC involvement in takeover regulation in the fourth wave was itself directed largely towards curtailing state regulation.¹⁸⁸ This Article, however, is not concerned with the causes of this SEC withdrawal but with its consequences.

IV. THE TRIUMPH OF DELAWARE OVER FEDERAL TAKEOVER REGULATION

Out of the SEC's shadow, the Delaware courts emerged as the nation's primary takeover regulator. Previously, as discussed above, the Delaware courts had a leading role—one founded on Delaware as the *situs* of incorporation for the majority of U.S. publicly traded companies. However, during the 1970s and 1980s, other state courts had notably and influentially acted with respect to takeover regulation.¹⁸⁹ This changed in the 1990s as the states largely began to toe the Delaware line on takeovers. Now, when other state courts acted, they largely followed existing takeover precedent established by the Delaware courts.¹⁹⁰ And Delaware was quite energetic in drawing and redrawing this line; during the fifth wave, the Delaware courts have repeatedly addressed new and old issues in response to developments. This has propelled the authority of the Delaware courts to new heights. The Delaware courts' expansionary takeover platform is the real takeover regulation story of the 1990s through today.

This is not to say that the Delaware courts have not acted during this time period to deregulate or loosen regulation with respect to certain aspects of takeovers. In fact, as will be seen in this Part, much of the Delaware courts' conduct was deregulatory, though the Delaware courts were careful to deregulate only in part, thereby maintaining a measure of oversight. Rather, the expansionary component referred to here is the Delaware courts' increasingly active involvement in takeover regulation. This section examines four main Delaware forays into takeover regulation, with a goal of contraposing the rise of the Delaware courts against the SEC's disappearance and setting forth the continued progress of takeover regulation despite the SEC's absence. The consequence is an in-

188. The SEC's position was often at odds with other organs of the Reagan Administration, which preferred a more abstentionist path. See *supra* note 122.

189. The regulation of going-privates, for example, was addressed by courts throughout the country. See Greene, *supra* note 58, at 496-506.

190. See, e.g., Guhan Subramanian, *The Drivers of Market Efficiency in Revlon Transactions*, 28 J. CORP. L. 691, 704 (2003) (stating that "most states outside Delaware follow *Revlon* [but] California, Indiana, Pennsylvania, New Jersey, North Carolina, Ohio, and Virginia have explicitly rejected *Revlon* through a combination of statutory law and case law"). The state legislatures were similarly docile. Some, notably Pennsylvania and Michigan, occasionally attempted to legislatively—and some would argue egregiously—influence the outcome of takeovers of particular significance to their state. See Kathryn Tully, *Pennsylvania Bails Out Sovereign Bancorp: US State's Decision to Pass a Law Protecting a Bank from Shareholder Activists Is Seen as a Setback for Investors*, EUROMONEY, Mar. 1, 2006, at 43 (reporting on a Pennsylvania law passed in 2006 and an amendment to a Michigan statute in 2003, both enacted to influence the outcome of a takeover involving a domestic corporation). But the state legislatures were more often content to tweak existing law, occasionally gathering enough energy to go a bit further and adopt new takeover statutes.

creasing disconnect between federal takeover regulation and the takeover conduct it today purports to regulate.

A. Takeover Standards

The Delaware courts in the fifth wave continued to address the appropriate standard governing an acquiree board's takeover decision. The Delaware Supreme Court had first addressed this issue in 1985 in *Revlon*.¹⁹¹ The *Revlon* court held that, upon a board decision to effect a change of control or breakup of the corporation, a board's fiduciary duties require it to obtain the highest price reasonably available for the corporation's stockholders.¹⁹² *Revlon* was decided when the SEC was making a full-court press to regulate takeover defenses and could also be spun as an attempt to stave off SEC action.¹⁹³ The SEC disappearance released this pressure valve, and it did not take long for the Delaware Supreme Court to act.

In the 1990 case of *Paramount Communications v. Time Inc.*¹⁹⁴ and the 1994 case of *Paramount Communications v. QVC Network Inc.*¹⁹⁵ the Delaware Supreme Court further defined the contours of and limited its previous holding in *Revlon*. The Delaware Supreme Court opinions in *Time* and *QVC* significantly weakened the *Revlon* decision by restricting *Revlon*'s application to a corporation's breakup or change of control.¹⁹⁶ Accordingly, in a post-*Time/QVC* world, except in a change of control context, antitakeover and transaction defenses do not implicate *Revlon* and are not subject to strict scrutiny.¹⁹⁷ These decisions also eliminated stock-for-stock acquisition transactions from review under *Revlon*'s higher standard.¹⁹⁸ In such transactions, both acquirer and acquiree stockholders share ownership of the merged entities and therefore control is almost always indeterminate. *Revlon* duties are accordingly inapplicable and the transaction subject to intermediate review under *Unocal*¹⁹⁹ except in atypical circumstances.²⁰⁰ This exclusion heavily influenced the structure of fifth wave transactions and spurred the widespread use of stock consideration; participants could now characterize their stock-for-stock transactions as "mergers of equals" and avoid application of *Revlon*.²⁰¹ More importantly, though, this pair of cases es-

191. *Revlon, Inc. v. MacAndrews & Forbes Holdings*, 506 A.2d 173 (Del. 1986).

192. *Id.* at 182.

193. *See supra* Part II.C.2.

194. 571 A.2d 1140 (Del. 1990).

195. 637 A.2d 34 (Del. 1994).

196. *See id.* at 47; *Time*, 571 A.2d 1140.

197. *See generally* Marc I. Steinberg, *Nightmare on Main Street: The Paramount Picture Horror Show*©, 16 DEL. J. CORP. L. 1, 15 (1991) (reviewing the interplay of *Time* and *Revlon* and arguing that "[t]he Delaware Supreme Court . . . narrowly constru[ed] *Revlon*'s scope").

198. *See, e.g., In re Santa Fe Pac. Corp. S'holder Litig.*, 669 A.2d 59, 70-71 (Del. 1995) (holding that *Revlon* duties do not apply where 67% of the corporation is acquired for stock and the remainder for cash).

199. The scope of intermediate review under *Unocal* is discussed *infra* at Part IV.B.

200. *See, e.g., Arnold v. Soc'y for Sav. Bancorp, Inc.*, 650 A.2d 1270, 1289-90 (Del. 1994) (holding *Revlon* duties inapplicable to a stock-for-stock transaction).

201. *See generally* James A. Fanto, *Braking the Merger Momentum: Reforming Corporate Law Governing Mega-Mergers*, 49 BUFF. L. REV. 249, 304-10 (2001) (surveying appli-

tablished the Delaware courts' willingness to relax takeover standards in light of the SEC's dormancy and, despite the deregulatory nature of its acts, the Delaware courts' primacy as the arbiter of the takeover decision.²⁰²

B. Takeover Defenses

The Delaware courts in the fifth wave also continued their active regulation of takeover defenses. Not surprisingly, given the SEC inattention, this regulation tended towards the permissive side while simultaneously preserving an oversight role for the Delaware courts. The first steps had been taken previously in the fourth wave in *Unocal*, which held that a Delaware court should review a board's defensive actions under an intermediate standard to ascertain whether they were "reasonable in relation to the threat posed."²⁰³ *Unocal*, like *Revlon*, could also be painted as a crafted response to the SEC's protakeover stance: the Delaware court's decision to regulate (and limit) takeover defenses an olive branch to account for the *Unocal* court's refusal, against SEC wishes, to find the exclusionary self-tender being considered therein as disproportional.²⁰⁴ It is therefore again not unexpected that, in the SEC's absence, the Delaware courts would act to limit the *Unocal* holding and expand a target board's defensive arsenal.

The Delaware Supreme Court first struck in the *Time* decision. The court not only restricted *Revlon's* scope but also interpreted *Unocal's* proportionality standard of review broadly by effectively upholding the "just-say-no" defense as a reasonable takeover response under *Unocal*.²⁰⁵ The SEC's fears in the fourth wave had now come to pass. Through use of the poison pill a target board could now, unless replaced, forestall a takeover by simply refusing to countenance an offer.²⁰⁶

Then, in 1995 the Delaware Supreme Court further relaxed *Unocal's* strictures on takeover defenses in *Unitrin, Inc. v. American General Corp.*²⁰⁷ *Unitrin*

cable regulatory standards for agreed stock-for-stock mergers); John C. Coffee, Jr., *Under the "Merger of Equals" Doctrine, Can a Target Board Always Favor a Friendly Suitor When a Second Bidder Makes a Higher, Unsolicited Offer?*, NAT'L L.J., Mar. 30, 1998, at B5 (observing that target boards can avoid application of *Revlon* scrutiny by structuring acquisition transactions so that they appear to be "a merger of equals" rather than an acquisition).

202. See Jeffrey N. Gordon, *Corporations, Markets, and Courts*, 91 COLUM. L. REV. 1931 (1991) (arguing that management and public opposition to takeovers influenced the Delaware court decision to relax the *Revlon* standard in *Time*).

203. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (1985).

204. See *id.* at 956-57. It didn't work. The SEC quickly acted to reverse this holding through adoption of the all-holders rule. See *supra* notes 151-53 and accompanying text.

205. See *Paramount Commc'ns v. Time Inc.*, 571 A.2d 1140, 1150 (Del. 1990).

206. As Professor Ronald Gilson has observed, this has created a presumptive bias for unsolicited offers to be resolved through proxy contests rather than via tender offers and market purchases. See Ronald J. Gilson, *Unocal Fifteen Years Later (and What We Can Do About It)*, 26 DEL. J. CORP. L. 491, 503-07 (2001). See also Joseph A. Grundfest, *Just Vote No: A Minimalist Strategy for Dealing with Barbarians Inside the Gates*, 45 STAN. L. REV. 857, 858 (1993) (observing that unsolicited bidders attempting to take over targets who have adopted a poison pill will "have to couple proxy contests with tender offers").

207. 651 A.2d 1361 (1995).

even further broadened the concept of proportionality under *Unocal* to provide target boards wide latitude in their ability to adopt strong, potentially preclusive takeover defenses.²⁰⁸ Thereafter, many an academic asserted that *Unocal* was dead—a strictly procedural formality.²⁰⁹ This was hyperbolic. The Delaware courts did continue to pay *Unocal* sacrificial heed on at least some level, employing it as a backstop to ensure continued Delaware supervision of takeovers. Accordingly, on the edges of *Unocal*, the Delaware courts, acting in their takeover supervisory role, repeatedly punished target boards who completely shut off a bid's potential for success, however remote, or who otherwise unfairly acted mid-contest to alter the rules of the game to the same effect.²¹⁰ But these decisions were islands in a sea of permissiveness. The Delaware courts in the fifth wave largely upheld the vast majority of takeover defensive action while still maintaining enough discretion and the threat of action to preserve their oversight role.²¹¹

208. See *id.* at 1387-90. See also *Moore Corp. v. Wallace Computer Servs.*, 907 F. Supp. 1545, 1563 (D. Del. 1995) (holding board refusal to redeem a poison pill was “within a ‘range of reasonableness’” under *Unocal*).

209. See, e.g., Robert B. Thompson & D. Gordon Smith, *Towards a New Theory of the Shareholder Role: “Sacred Space” in Corporate Takeovers*, 80 TEX. L. REV. 261, 284-86 (2001) (asserting that *Unocal* is “dea[d]”).

210. Thus, in *Mentor Graphics Corp. v. Quickturn Design Systems*, 728 A.2d 25 (Del. Ch. 1998), *aff'd sub nom.*, *Quickturn Design Sys., Inc. v. Shapiro*, 721 A.2d 1281 (Del. 1998), the Delaware Court of Chancery struck down a poison pill as disproportionate under *Unocal*. *Id.* at 44-52. See generally Peter V. Letsou, *Are Dead Hand (and No Hand) Poison Pills Really Dead?*, 68 U. CIN. L. REV. 1101 (2000). Then, in *Chesapeake Corp. v. Shore*, 771 A.2d 293 (Del. Ch. 2000), the Court of Chancery held that a bylaw provision adopted mid-takeover battle, which effectively frustrated an unsolicited bidder after its successful proxy battle, was not sustainable under *Unocal*. See *id.* at 342-44.

211. Since *Unitrin*, the Delaware courts have held four takeover defense responses to be disproportional under the *Unocal* standard. All except *Omnicare* were decided in the Court of Chancery. See *Omnicare Inc. v. NCS Healthcare*, 818 A.2d 914 (Del. 2003); *Chesapeake Corp.*, 771 A.2d at 293; *Mentor Graphics*, 728 A.2d at 25; *Carmody v. Toll Bros.*, 723 A.2d 1180 (Del. Ch. 1998). *Unitrin* itself overturned a finding by the Court of Chancery that the takeover defenses adopted therein were invalid under *Unocal*. See *In re Unitrin, Inc. S'holders Litig.*, Civ. A Nos. 13656 & 13699, 1994 WL 698483 (Del. Ch. Oct. 13, 1994). The Delaware courts also initiated periodic review of transactions under the holding of *Blasius Industries v. Atlas Corp.*, 564 A.2d 651, 659-61 (Del. Ch. 1988). The standard in *Blasius* is applied when “the primary purpose of the board’s action is to interfere with or impede exercise of the shareholder franchise and the stockholders are not given a full and fair opportunity to vote.” *Williams v. Geier*, 671 A.2d 1368, 1376 (Del. 1996) (quoting *Stroud v. Grace*, 606 A.2d 75, 92 (Del. 1992)) (internal quotations omitted). There had been some debate in the 1990s concerning the continued existence of this standard and its fit with the *Unocal* standard. But the Delaware Supreme Court reaffirmed its validity in *MM Cos. v. Liquid Audio, Inc.*, 813 A.2d 1118 (Del. 2003), when the court applied a *Blasius* analysis within an application of the *Unocal* standard to overturn the Liquid Audio board’s expansion of itself from five to seven members, an action which effectively defeated a hostile proxy contest. *MM Cos.*, 813 A.2d at 1132. The interplay of *Unocal* and *Blasius* is discussed extensively in Harry G. Hutchison, *Director Primacy and Corporate Governance: Shareholder Voting Rights Captured by the Accountability/Authority Paradigm*, 36 LOY. U. CHI. L.J. 1111, 1172-85 (2005).

C. Transaction Defenses

The widespread use of the stock-for-stock merger structure in the fifth wave also heralded the increased use of the lock-up transaction defense.²¹² This trend was buoyed by the Delaware courts in 1997 in *Brazen v. Bell Atlantic Corp.*²¹³ In *Brazen*, the Delaware Supreme Court upheld the validity of a \$550 million termination fee agreed in the negotiated stock-for-stock merger-of-equals transaction between Bell Atlantic and NYNEX.²¹⁴ The court refused to scrutinize under fiduciary duty principles the board decision to agree to the fee, instead applying a liquidated damages contractual analysis to uphold the fee under reasonableness grounds.²¹⁵ Henceforth, acquirers agreeing to transactions without the specter of another bid would have wide latitude to agree to potentially preclusive lock-ups.²¹⁶ The effect was to make intervening bids more difficult and costly. This also gave a substantial, potentially preclusive, head start to an acquiree board's choice of acquirer.²¹⁷

Then, in *Omnicare, Inc. v. NCS Healthcare*,²¹⁸ the Delaware courts limited the ability of a majority stockholder to agree to a stock lock-up when the acquiree had agreed to a "force-the-vote" provision.²¹⁹ The court held that, under

212. In their study of lock-ups, Professors John C. Coates IV and Guhan Subramanian found that "[i]n friendly U.S. mergers greater than \$50 million in value, lockups appeared in 80% of deals in 1998, compared to 40% of deals a decade ago." See John C. Coates IV & Guhan Subramanian, *A Buy-Side Model of M&A Lockups: Theory and Evidence*, 53 STAN. L. REV. 307, 310 (2000). They also found that "all-stock deals are much more likely to have stock lockups than cash deals (39% vs. 12%) or deals involving mixed consideration (18%), but are not more likely to have breakup fees than cash deals (46% vs. 47%) or mixed deals (55%)." *Id.* at 391-92.

213. 695 A.2d 43 (Del. 1997).

214. *Id.* at 45. However, the supreme court's holding was arguably at odds with its decision in *Time* which held that "structural safety devices" in non-*Revlon* transactions were to be reviewed under *Unocal's* proportionality standard. See *Paramount Commc'ns v. Time Inc.*, 571 A.2d 1140, 1151 (Del. 1990).

215. See *Brazen*, 695 A.2d at 45.

216. See, e.g., *In re IXC Commc'ns Inc. S'holders Litig.*, Nos. C.A. 17324 & C.A. 17334, 1999 WL 1009174, at *10 (Del. Ch. Oct. 27, 1999) ("[E]nhanced judicial scrutiny does not apply . . . [as] [n]either the termination fee, the stock option agreements nor the no-solicitation provisions are defensive mechanisms instituted to respond to a perceived threat to a potential acquirer."). The Delaware courts were equally sanguine about transactions on the other end of the playing field, those in *Revlon*-land. In two decisions rendered in 2001 and 2004, respectively, *In re Pennaco Energy, Inc. Shareholders Litigation*, 787 A.2d 691, 705-06 (Del. Ch. 2001), and *In re MONY Group Shareholder Litigation*, 852 A.2d 9, 18-24 (Del. Ch. 2004), the Delaware courts gave broad discretion to an acquiree's ability to agree to lock-ups in a change of control context.

217. Professors Coates' and Subramanian's empirical research has led them to conclude that "when another bidder is present, a lockup more than doubles the likelihood of completion for the first bidder." Coates & Subramanian, *supra* note 212, at 348. On this basis, they argue that "foreclosing lockups do exist, and, more generally, that lockups do influence bid outcomes." *Id.* at 389.

218. 818 A.2d 914 (Del. 2003).

219. This provision, if agreed to by the acquiree, requires the target to hold a vote on the acquisition transaction even if the acquiree board of directors decides to withdraw its recommendation for the transaction. DEL. CODE ANN. tit. 8, § 251(c) (2006). Meanwhile, the stockholder lock-up itself typically obligates the stockholder parties to irrevocably vote in favor of the acquisition. These two provisions interact to effectively sew up the acquisition

Unocal, this certainty was deficient; a contractually foreclosing lock-up was henceforth required to be subject to a “fiduciary-out” clause whereby the acquiree board could terminate the transaction and the lock-up if, in light of subsequent developments, including a competing offer, the board’s fiduciary duties required it to.²²⁰ *Omnicare* was yet another incursion; it now put another category of takeover-related conduct—stockholder lock-ups—under supervision of the Delaware courts.²²¹

Omnicare was also the most significant and controversial Delaware court decision in favor of stockholder choice since the *Revlon* decision itself.²²² In the end, though, the Delaware courts never addressed the fundamental question of stockholder lock-ups per se, and their use post-*Omnicare* remains widespread, albeit subject to the restrictions set forth in *Omnicare* and the oversight of the Delaware courts. Thus, the significance of *Omnicare* for this Article is another instance of the Delaware courts seizing the takeover regulator mantle. Their willingness to confront, regulate, and address the takeover issues of the day thereby redefined material elements of takeover law and influence takeover tactics and strategy.

D. Going-Privates

Going-private transactions also continued to prominently figure in the jurisprudence of the Delaware courts. The Delaware Supreme Court had previously, in the fourth wave, refined its holding in *Singer* to discard the “business purpose” test. The court held that going-private transactions should be reviewed solely under *Singer*’s “entire fairness” prong.²²³ This changed in the new millennium. In *In re Pure Resources, Inc., Shareholders Litigation*,²²⁴ the Court of Chancery, per Vice Chancellor Strine, held that the “entire fairness” standard was applicable only to merger transactions, not tender offers.²²⁵ *Pure Resources*

for an acquirer no matter the will of the other stockholders; there is no ability to escape. If the lock-up does not extend to a dispositive number of shares, it still tips the scales in favor of the acquiree transaction.

220. *Omnicare*, 818 A.2d at 934-36.

221. The Court of Chancery strictly construed the scope of *Omnicare* in *Orman v. Cullman*, No. Civ.A. 18039, 2004 WL 2348395 (Del. Ch. Oct. 20, 2004). *Orman* relied heavily on *Brazen* to hold that a stockholder lock-up can be used to reduce the stockholder choice to a binary one: either the transaction at hand or no transaction—even in light of *Omnicare*, a stockholder lock-up can still under Delaware law forestall other alternatives. *Id.* at *5.

222. See Tamara Loomis, *Beware Delaware: The State’s Recent Supreme Court Decisions Make Waves*, N.Y. L.J., May 15, 2003, at 5 (reporting prostockholder nature of the decision has “sent shock waves through the corporate legal community”).

223. See *Weinberger v. UOP, Inc.*, 457 A.2d 701, 715 (Del. 1983). The abandonment of the business purpose test could also be viewed as a response to the implementation by the SEC of its own going-private rules; Delaware was now at liberty to relax its own standard. In *Kahn v. Lynch Communication Systems*, 638 A.2d 1110 (Del. 1994), the Delaware Supreme Court further refined the *Weinberger* holding. It held that approval by an acquiree special committee did not obviate the Delaware court’s required entire fairness review but merely shifted the burden of proof from the acquirer to the challenging stockholders. *Id.* at 1117.

224. 808 A.2d 421 (Del. Ch. 2002).

225. *Id.* at 444.

held that, provided certain procedures were followed, going-private transactions effected via tender offer would be reviewed by the Delaware courts under the business judgment rule and not a higher standard.²²⁶ Moreover, approval by a special committee or entire board of the acquiree was not a requirement for this relaxed review.²²⁷ This was a significant side-step for the Delaware courts because it not only offered a path to deregulate going-private tender offer transactions but effectively removed the Delaware courts from supervision of such transactions.²²⁸ Going forward and until a Delaware Supreme Court decision to the contrary, rational acquirers in going-privates will preferentially escape Delaware court review of their transactions by employing a tender offer structure.²²⁹

E. Federal Takeover Regulation Circa 2007

We continue to ride the fifth wave of takeover activity. During this time, the Delaware courts have emerged as the nation's primary takeover regulator: actively involved, regulating almost every aspect of the takeover. Furthermore, while the Delaware courts sometimes acted to deregulate, they maintained their supervision of takeovers by resorting to another of the various skeins of height-

226. *Id.* at 446.

227. *Id.* at 446-47. See also *In re Siliconix Inc. S'holders Litig.*, No. Civ. A. 18700, 2001 WL 716787, at *6 (Del. Ch. June 19, 2001) (stating that "unless coercion or disclosure violations can be shown, no defendant has the duty to demonstrate the entire fairness of this proposed tender transaction"). See generally Jason M. Quintana, *Going Private Transactions: Delaware's Race to the Bottom?*, 2004 COLUM. BUS. L. REV. 547 (analyzing recent developments in Delaware going-private jurisprudence through a state charter competition lens).

228. The path was hewn in *Glassman v. Unocal Exploration Corp.*, 777 A.2d 242, 243 (Del. 2001). In *Glassman*, the Delaware Supreme Court held that "absent fraud or illegality," a short-form merger was subject to review under the business judgment rule, rather than an entire fairness standard, and specifically, the court held that "appraisal is the exclusive remedy available to a minority stockholder who objects to a short-form merger." *Id.* at 248. See also *In re Unocal Exploration Corp. S'holders Litig.*, 793 A.2d 329 (Del. Ch. 2000) (holding entire-fairness review is not implicated in short-form mergers). In Delaware, once a stockholder acquires ninety percent or more of a corporation's stock, it can cash out the remaining minority without a stockholder vote. DEL. CODE ANN. tit. 8, §253 (2006). Accordingly, *Glassman* and *Pure Resources* provide a clear way for a controlling stockholder to initiate a tender offer in a going-private, obtain ninety percent of a corporation's stock, and then cash out the minority without a stockholder vote and having to undergo substantive review for entire fairness.

229. See Christopher A. Iacono, Comment, *Tender Offers and Short-Form Mergers by Controlling Shareholders Under Delaware Law: The "800-Pound Gorilla" Continues Unimpeded—In re Pure Resources, Inc., Shareholders Litigation*, 28 DEL. J. CORP. L. 645, 671 (2003) ("Because of the Delaware Court of Chancery's decision in *Pure Resources*, the position of the tender offer followed by a short-form merger has been secured as the most favorable transaction for controlling shareholders."). In *In re Cox Communications, Inc., Shareholders Litigation*, 879 A.2d 604 (Del. Ch. 2005), Vice Chancellor Strine suggested "a relatively modest alteration of *Lynch*" in which "if a controller proposed a merger, subject from inception to negotiation and approval of the merger by an independent special committee and a Minority Approval Condition, the business judgment rule should presumptively apply." *Id.* at 643-44 (footnote omitted). The only modesty here is Vice Chancellor Strine's understatement; his dictum calls into question the status of *Lynch* and even *Weinberger*.

ened review previously established.²³⁰ And, if the mainstay takeover standards did not suit, the Delaware courts were not shy about conjuring up other judicial standards and statutes to scrutinize these transactions.²³¹ Additionally, only once did the Delaware courts act to fully deregulate—the Court of Chancery’s decision in *Pure Resources*, and its holding is still subject to consideration by the Delaware Supreme Court.²³² The result was a spaghetti of holdings and standards in which scholars struggled to find doctrinal coherence and order.²³³ However, one explanation for this disarray is to view these decisions through this Article’s prism: the Delaware’s courts’ labors to maintain a firm regulatory and supervisory grip even when ostensibly acting in a deregulatory fashion.²³⁴ These fifth wave decisions generally preserved and extended the ability of target officers, directors, and controlling stockholders to d

230. Thus, in *Chesapeake Corp. and Mentor Graphics, Revlon* duties were not implicated since *Time* and *QVC* had restricted their applicability, yet the courts still could invoke the *Unocal* standard to sustain their holdings. Similarly, despite the confines *Brazen* previously placed on court review of lock-ups, the Delaware courts could still apply *Unocal* to decide *Omnicare*.

231. See, e.g., *ACE Ltd. v. Capital Re Corp.*, 747 A.2d 95, 108-09 (Del. Ch. 1999) (holding that a board’s fiduciary duties of care and loyalty require the court to enjoin enforcement of a contractual no-talk provision); *Phelps Dodge Corp. v. Cyprus Amax Minerals Co.*, Nos. Civ. A. 17398, Civ. A. 17383, Civ. A. 17427, 1999 WL 1054255, at *1 (Del. Ch. Sept. 27, 1999) (holding that it may constitute a breach of the board’s duty of care to agree to a no-talk provision in a merger agreement); *Quickturn Design Sys. v. Shapiro*, 721 A.2d 1281, 1292 (Del. 1998) (holding adoption of dead-hand poison pill violative of 8 Del. C. § 141(a) (1998)). See also *supra* note 211 (discussing application of *Blasius* standard in *Liquid Audio*).

232. See *supra* notes 224-29 and accompanying text. Some predict that, if it considers the matter, the Delaware Supreme Court would overrule *Pure Resources* and maintain its previous consistent bias towards court supervision of going-private transactions and general refusal to wholly deregulate takeover decisions. See Lawrence Lederman & Faith Stevelman Kahn, *Conflict Irresolution*, DAILY DEAL, Sept. 19, 2005, available at 2005 WLNR 14646788 (“In a fresh look [at going-private transactions], we can expect the [Delaware] Supreme Court to retain entire fairness review, regardless of the form of the transaction, and make the tender offer format conform to mergers rather than the other way around.”). Others, perhaps more cynical, dispute this prognostication. See Iacono, *supra* note 229, at 670 (stating that the Delaware Supreme Court “would most likely affirm that the entire fairness standard is inapplicable to tender offers made by controlling shareholders”).

233. See, e.g., Marcel Kahan, *Paramount or Paradox: The Delaware Supreme Court’s Takeover Jurisprudence*, 19 J. CORP. L. 583, 584 (1994) (stating that commentators “have referred to the [Delaware] [S]upreme [C]ourt’s takeover jurisprudence as mush and mud; disparaged the court for waffling and wavering; criticized its opinions for drawing distinctions ‘without foundation,’ being ‘equivocal,’ and lacking clarity”); Skeel, *supra* note 165, at 166 (“From a doctrinal perspective, *Time*] and *QVC* are extremely difficult to reconcile.”). See generally William T. Allen et al., *Function over Form: A Reassessment of Standards of Review in Delaware Corporation Law*, 26 DEL. J. CORP. L. 859, 864 (2001) (reviewing the standards of review and conduct promulgated by the Delaware courts and observing that “new standards of review [have] proliferated”).

234. There is a subtle interplay here between the Delaware courts’ shifting standards and regulation and the maintenance of such standards and regulations. Specifically, swings in these standards and regulation themselves can be viewed as a function of the Delaware courts as a regulating entity. See Griffith & Steele, *supra* note 11, at 2 (noting “the ability of state corporate law, especially in Delaware, to alternate between lax and stringent regulation, shifting between hard-edged rules and fuzzy standards” in response to crises and other public developments).

irect the takeover decision.²³⁵ This relaxation in standards can also be characterized as furthering promanagement ends, including the ability of management to entrench itself, to the detriment of stockholder choice.²³⁶ All of this conduct was consequential, but particularly so since in the fifth wave the Delaware courts became the sole regulator of takeovers. Thus, it no longer mattered that the 1980s SEC would most likely have vigorously opposed these Delaware court holdings or that the Delaware courts would therefore likely have not treaded so far in favoring corporate management interests in light of such opposition. The SEC was nowhere in sight—a state that still exists today.

V. THE FAILURE OF FEDERAL TAKEOVER REGULATION

The SEC abstention not only permitted a new, Delaware-driven takeover code to emerge, it also engendered an increasing mismatch between the federal takeover code and the takeovers that it was created to govern. The federal takeover code had largely been established in the 1960s through the Williams Act and built upon by the SEC through the 1980s. This model had been constructed for a time when acquisitions were perpetuated in another manner, takeover tactics and strategies different, takeover and transaction defenses virtually nonexistent, capital markets less well-developed, and research on the validity and utility of various takeover substantive, procedural, and disclosure requirements unavailable or preliminary. Yet the federal takeover rules have remained static in the face of these developments as the SEC failed to adapt them to changed circumstance. The result is an outdated federal takeover code. Moreover, the takeover laws promulgated by the Delaware courts have arguably exacerbated these federal failings and altered the requirements for future, necessary federal action. This Part traces these shortfalls by illuminating some of the more trenchant examples.

A. *The Failure of the Williams Act*

The following three examples illustrate Williams Act's outdatedness due to the substantially changed takeover environment existent today.

235. See generally Jill E. Fisch, *The Peculiar Role of the Delaware Courts in the Competition for Corporate Charters*, 68 U. CIN. L. REV. 1061, 1067 (2000) (“[E]vidence suggests that, although Delaware is successful in attracting charters, its law is not optimal. . . . Delaware law appears to favor management interests at the expense of shareholder interests.”). Unfortunately, not all of Delaware’s conduct fits neatly into this box. Certainly, *Kahn* and *Omicare* are outliers. But they can still be shoehorned into this Article’s thesis if explained as an assertion of regulatory authority by the Delaware courts.

236. Thus, *Time* and *QVC* cut back the compass of *Revlon* duties, thereby increasing the power of target directors to reject, in the stead of stockholders, a takeover; *Unitrin* enlarged the play-book of board permitted takeover defensive conduct under *Unocal*; *Brazen* expanded a board’s capacity to contractually grant lock-ups inhibitory and possibly preclusive of other alternative, stockholder preferred transactions; and *Pure Resources* enhanced controlling stockholders’ and management’s ability to take a corporation private and freeze out minority stockholders. See *supra* Parts IV.A-IV.D.

1. Offer Period

In 1979, the SEC set the minimum offer period for a full tender offer at twenty business days.²³⁷ The purpose was to finish off the “Saturday Night Special” and slow unsolicited, coercive offers which forced overly hasty stockholder decisions to tender.²³⁸ Today, short-period offers of this nature are precluded by the poison pill, which effectively necessitates a concomitant and time-consuming proxy contest if the target board does not consent to the proposed transaction.²³⁹ This has rendered the federal minimum offer period redundant and unnecessary to the extent it purports to protect stockholders from the coercive aspects of short-period tender offers. Thus, the original rationale underpinning this rule no longer exists.

In this absence, there are arguments that this period is too short, too long, or even unnecessary. First, the allotted period is arguably insufficient to permit stockholder consideration of the transaction and for alternatives to emerge. The period should rather be that of two to three months in a merger transaction or even longer.²⁴⁰ This is an argument that has been put forth for decades.²⁴¹ But it has stronger purchase in today’s takeover environment since an acquirer can now agree to a tender offer structure with a preselected acquirer which includes potentially preclusive lock-up provisions that favor and advantage this acquirer.²⁴² Accordingly, an acquirer’s ability to select a shorter tender offer over a merger period in the presence of lock-ups is yet another arguably unneeded way for an acquirer to incrementally favor a chosen acquirer.²⁴³

Alternatively, reasons militate towards either a shorter mandatory period or none at all. In the advent of the poison pill, truly hostile takeovers are no longer possible,²⁴⁴ and it could be argued that the period for an any-and-all tender offer is one that should or could be negotiated and set between the acquirer and the acquirer as a bargain between two commercially sophisticated, equally footed parties. Furthermore, application of mainstay fiduciary duty principles could

237. 17 C.F.R. § 240.14e-1(a) (1980).

238. See Prentice & Langmore, *supra* note 125, at 435 n.291.

239. See *supra* note 206.

240. This could mitigate the potentially coercive nature of tender offers. See generally Lucian Arye Bebchuk, *The Pressure to Tender: An Analysis and a Proposed Remedy*, 12 DEL. J. CORP. L. 911 (1987); Louis Lowenstein, *Pruning Deadwood in Hostile Takeovers: A Proposal for Legislation*, 83 COLUM. L. REV. 249, 307-09 (1983).

241. See e.g., Arthur J. Goldberg, *Regulation of Hostile Tender Offers: A Dissenting View and Recommended Reforms*, 43 MD. L. REV. 225, 232-33 (1984) (arguing for a mandatory freeze-period of 120 days for tender offers to permit competing offers to emerge and adequate antitrust review); Lowenstein, *supra* note 240, at 317 (proposing a six-month offer period for unsolicited tender offers which are not accepted by a target board). This argument is supported by the common practice in tender offers for stockholders, particularly stockholders who are arbitrageurs and represent a significant if not majority of tendering shares, to wait until the last day to tender despite the existence of withdrawal rights. James R. Pagano, Note, *The Constitutionality of Second Generation Takeover Statutes*, 73 VA. L. REV. 203, 228 n.146 (1987).

242. See *supra* Part IV.C.

243. This is evidenced by the rarity of acquirers and acquirees contractually agreeing to a tender offer period that is longer than the statutory minimum.

244. See *supra* note 206 and accompanying text.

function to protect stockholders from a board's attempt to coerce its own stockholders through a curtailed offer period.²⁴⁵ Regulation is therefore unnecessary, and its removal or curtailment possibly a boon to takeover activity by speeding up these acquisitions to a measured degree and inducing an increased rate of bidding.²⁴⁶

2. *Outside Purchases*

Former Rule 10b-13 (now redesignated Rule 14e-5) prohibits bidder purchases outside of a tender offer from the time of announcement until completion.²⁴⁷ The primary reason put forth by the SEC for barring these purchases in 1969 was that they "operate[] to the disadvantage of the security holders who have already deposited their securities and who are unable to withdraw them in order to obtain the advantage of possible resulting higher market prices."²⁴⁸ This is no longer correct; bidders are now obligated to offer unlimited withdrawal rights throughout the offer period.²⁴⁹ Moreover, Rule 10b-13 was issued at a time when targets had no ability to defend against these bidder purchases. They were yet another coercive and abusive tactic whereby the bidder could obtain control through purchases without the tender offer, thereby exerting pressure on stockholders to tender before the bidder terminated or completed its offer on the basis of these purchases.²⁵⁰ This is not feasible today. Poison pills and second and later generation state takeover statutes act to restrict these purchases to

245. The fifteen-day waiting period for cash tender offers under the HSR Act would still typically apply to impose a *de facto* minimum waiting period. See 16 C.F.R. § 803.10 (2006).

246. Professors Jarrell & Bradley have also argued that an extended period is detrimental to bidder incentives to bid because it permits other prospective bidders to free-ride on the initial bidder's knowledge and reputational investment. See generally Gregg A. Jarrell & Michael Bradley, *The Economic Effects of Federal and State Regulations of Cash Tender Offers*, 23 J.L. & ECON. 371 (1980). This and other arguments for shortening or eliminating the period are in line with studies finding that takeover premiums and the number of bids actually declined following the adoption of the Williams Act. See Kevin S. Nathan & Terrence B. O'Keefe, *The Rise in Takeover Premiums: An Exploratory Study*, 23 J. FIN. ECON. 101, 115-18 (1989) (finding that mean takeover premiums declined in the six years immediately following the Williams Act and then increased in 1974). For general criticism of the Williams Act on economic efficiency grounds, see Daniel R. Fischel, *Efficient Capital Market Theory, the Market for Corporate Control, and the Regulation of Cash Tender Offers*, 57 TEX. L. REV. 1 (1978).

247. 17 C.F.R. § 230.14e-5 (2006). See generally M&A Release, *supra* note 51, at 82,608-12.

248. Rule 10b-13 Release, *supra* note 51, at 83,708.

249. 17 C.F.R. § 230.14d-7.

250. The SEC stated in the 10b-13 Release that such purchases could defeat the tender offer, either by driving the market price above the offer price or by otherwise reducing the number of shares tendered below the stated minimum. Alternatively, they could further the tender offer by raising the market price to the point where ordinary investors sell in the market to arbitrageurs, who in turn tender.

Rule 10b-13 Release, *supra* note 51, at 83,708. The SEC here appeared to misapprehend the relationship of arbitrageurs and stockholders in takeovers. Even in the 1960s, many stockholders sold in the market immediately upon transaction announcement. See generally Frederick B. Henry, *Activities of Arbitrageurs in Tender Offers*, 119 U. PA. L. REV. 466 (1971).

threshold noncontrolling levels without target approval.²⁵¹ In the wake of these developments, the original reasons underlying the promulgation of Rule 10b-13 no longer exist.

Moreover, Rule 14e-5, by its terms, acts to confine bidder purchases to periods prior to offer announcement.²⁵² However, a bidder's capacity to make preannouncement acquisitions has been adversely effected by a number of subsequent changes in the takeover code, such as the Hart-Scott-Rodino waiting and review period requirements.²⁵³ These have combined to chill a bidder's ability to make preannouncement acquisitions or forthrightly precluded such purchases. Consequently, one study has recently reported that at least forty-seven percent of initial bidders have a zero equity position upon entrance into a contest for corporate control.²⁵⁴

A bidder's preannouncement purchase of a stake in the target, known as a toehold, can be beneficial. The toehold purchase defrays bidder costs, incentivizes the bidder to complete the takeover, and reduces free-rider and information asymmetry problems.²⁵⁵ This can lead to higher and more frequent bids. Meanwhile, market purchases amidst a tender offer can provide similar benefits while providing market liquidity and confidence for arbitrageurs to fully act in the market.²⁵⁶

Since the initial premise for this rule is no longer valid and recent research supports encouragement of these purchases, the SEC should accordingly consider loosening restrictions on bidder toeholds and postannouncement purchases. This deregulation may be particularly appropriate in order to defray bidder sunk costs if a regime for corporate control transactions which prohibits or limits lock-ups is ever adopted.²⁵⁷

251. For a discussion of the limitations on acquisitions placed by state takeover statutes, see Pinto, *supra* note 156, at 713-16.

252. 17 C.F.R. § 230.14e-5.

253. See generally George Cummings, Jr. et al., *HSR Compliance Guidelines, in VENTURE CAPITAL: GETTING FINANCING IN A CHANGING ENVIRONMENT* (PLI Corp. Law and Practice, Course Handbook Series No. B0-017M, Sept. 2001).

254. Sandra Betton & B. Espen Eckbo, *Toeholds, Bid Jumps, and Expected Payoffs in Takeovers*, 13 REV. FIN. ST. 841 (2000).

255. See Jeremy Bulow et al., *Toeholds and Takeovers*, 107 J. POL. ECONOMY 427 (1999) (arguing that toeholds mitigate the problem of asymmetric information); Sanford J. Grossman & Oliver D. Hart, *Takeover Bids, the Free-Rider Problem and the Theory of the Corporation*, 11 BELL J. ECON. 42-64 (1980). See also Jun Qian, *Toehold Acquisitions, Market Reaction, and Corporate Control* (Apr. 2001), <http://ssrn.com/abstract=270098> (surveying the literature and arguing that a toehold strategy does not solve free-rider problems).

256. The SEC itself even noted this potential in the Rule 10b-13 adopting release. See 10b-13 Release, *supra* note 51, at 83,708. See generally Ronald J. Gilson & Reinier H. Kraakman, *The Mechanisms of Market Efficiency*, 70 VA. L. REV. 549 (1984) (discussing informational trading practices as fostering market efficiency).

257. A regime which allows for bidder toeholds is another way to compensate bidders for due diligence, reputational, and other bid-related investments in the face of an auctioneering regime which encourages competing bids and limits the ability of lock-ups to provide such compensation. See generally Frank H. Easterbrook & Daniel R. Fischel, *Auctions and Sunk Costs in Tender Offers*, 35 STAN. L. REV. 1 (1982); Edith Hotchkiss et al., *Holdups, Renegotiation, and Deal Protection in Mergers* (July 2005), <http://ssrn.com/abstract=620442>. But Professor Guhan Subramanian has found that em-

Bidder toeholds and off-market purchases, however, do have a potentially corrosive effect if the stake is significant.²⁵⁸ To dampen this possibility, a relaxation of these purchase rules could be combined with provisions similar to those in the U.K. Takeover Code which permit pre- and postannouncement purchases but require the bidder to pay for a set period thereafter no less than that price paid for all subsequently acquired shares.²⁵⁹ Alternatively, the SEC could wholly deregulate and leave the possibility or actuality of bidder toeholds and postannouncement purchases to be regulated by targets through a low-threshold poison pill or other takeover defenses as well as through bargaining with potential bidders.

Finally, Rule 14e-5 has never applied to bar purchases while a merger transaction is pending.²⁶⁰ Presumably, this path dependency was set in 1969 because a bidder in a merger situation requires acquiree agreement; the acquiree can therefore contractually respond to and regulate this conduct. But whatever the reason, today a bidder who runs a proxy contest without a tender offer is permitted postannouncement purchases during the contest.²⁶¹ Unsolicited bidders will therefore initially characterize their offers as mergers in order to leave the option of such purchases. The result is preferential bias towards mergers over tender offers, discrimination which no longer seems sensible in a world where a takeover transaction will not succeed unless the original or replaced acquiree board agrees to it. Any prohibition on outside purchases should apply to both merger and tender offer structures or to neither.

3. *Going-Privates*

The federal going-private rules do not apply if stock consideration is offered instead of cash.²⁶² The SEC-professed reason for this exception is that the protections of the going-private rules are unnecessary, since the minority stockholder continues to maintain an interest in the going-concern on an equal basis as the affiliated stockholders.²⁶³ The reasoning has always been tenuous, as the coercive elements of a going-private remain, no matter the form of considera-

pirical evidence supports the conclusion that the *Revlon* auctioneering rule did not reduce bidder incentives to search. Subramanian, *supra* note 190, at 704-13. This may have been due to the use of lock-ups under Delaware law and the compensation they still provided with respect to bidder sunk costs.

258. Terence L. Blackburn, *The Regulation of Market Sweeps in Connection with Tender Offers*, 58 GEO. WASH. L. REV. 619, 632 (1990) (arguing that market sweeps deny stockholders the opportunity present in a tender offer "to evaluate the likelihood of success of the tender offer on virtually a daily basis").

259. See The Panel on Takeovers and Mergers, THE CITY CODE ON TAKEOVERS AND MERGERS, at Rules 6 & 11 (2006) [hereinafter CITY CODE].

260. See 17 C.F.R. § 230.14e-5 (2006).

261. In most cases, the acquiree will have the acquirer contractually agree to abstain from such purchases upon agreement to a merger. This is yet another argument for this prohibition to be one bargained between acquiree and acquirer.

262. See 17 C.F.R. § 230.13e-3(g)(2).

263. The SEC specifically stated in the Going-Private Adopting Release that it "believes that such transactions are also outside the purpose of Rule 13e-3 since all holders of that class of security are on an equal footing and are permitted to maintain an equivalent or enhanced equity interest." Going-Private Adopting Release, *supra* note 68, at 82,127.

tion. The propriety of this exception is further suspect in the wake of the *Pure Resources* decision. Now, an acquirer, through a first step exchange offer structure, can exploit this federal loophole and side-step all of the prior requirements, both federal and state, for going-private transactions.²⁶⁴ Moreover, the further safeguard of dissenters' rights is typically unavailable in stock-for-stock going-private transactions.²⁶⁵ These likely were not consequences that the SEC expected when it promulgated its own federal regulation of going-privates.

More generally, the SEC going-private rules were issued after the *Singer* decision.²⁶⁶ The SEC presumably structured its own archetype to work in tandem with this Delaware holding. Yet the *Singer* holding has been trimmed by the Delaware Supreme Court and largely gutted by *Pure Resources*.²⁶⁷ Moreover, Delaware has still yet to substantively address the re-emergent problems with management-sponsored buy-outs often made in tandem with, and financed by, private equity firms to the disadvantage of unaffiliated stockholders. These developments, as well as the loophole noted above, arguably render outdated the current federal going-private rules. They no longer act to prevent and mitigate the abusive practices in going-privates in the manner in which they were initially intended. This is a claim supported by recent empirical findings that minority stockholders in going-privates receive lower compensation than they would in traditional corporate control transactions.²⁶⁸ Going-privates are thus an area ripe for the SEC to update its rules.

4. Other Examples

There are numerous other examples. The continued rationale for the prohibition on short and hedged tendering in partial offers is questionable in light of

264. For a discussion of the *Pure Resources* holding, see *supra* notes 224-29 and accompanying text.

265. Delaware appraisal rights are generally unavailable to any stockholder in a merger or consolidation where the stock is either (1) listed on the stock exchange or quoted on an inter-dealer quotation system or (2) held of record by more than 2,000 holders and where the consideration is stock of the corporation surviving or resulting from such merger or consolidation. DEL. CODE ANN. tit. 8, § 262(b)(2)b (2006).

266. See *supra* notes 66-70 and accompanying text.

267. Here, the "trimming" I refer to is Weinberger's limitation of the *Singer* test to the "entire fairness" prong. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 715 (Del. 1983).

268. See generally Subramanian, *supra* note 164 (arguing that Delaware law on going-privates permits inefficient going-private transactions and deters efficient going-private transactions). In a companion piece, Professor Subramanian conducted an empirical study of the treatment of minority stockholders in tender offer and merger going-private transactions. He found that minority stockholders receive a lower premium in going-private tender offer transactions than in mergers. See Guhan Subramanian, *Post-Siliconix Freezeouts: Theory, Evidence and Policy* (Harv. L. Sch. John M. Olin Ctr. for L., Econ., & Bus., Discussion Paper No. 472, 2004), available at http://www.law.harvard.edu/programs/olin_center/corporate_governance/papers.htm. Moreover, the arguable need for further regulation is supported by a recent study by Dealogic which found that "[t]he premium that management-led buyers paid to shareholders was, on average, just shy of 20 percent . . . compared to the 27.5 percent average premium that shareholders received when a rival or a private equity firm unaffiliated with management was the buyer." Andrew Ross Sorkin, *Investors, Watch Your Wallets if Managers Lead the Buyout*, N.Y. TIMES, July 30, 2006, at C33.

the current deeply liquid capital markets.²⁶⁹ SEC disclosure standards are arguably not copious enough or require disclosure that is no longer appropriate or applicable to the present paradigm.²⁷⁰ Meanwhile, wholesale repeal of the all-holders/best price rule may be appropriate in today's takeover environment in order to permit transaction participants to order their own economic rights.²⁷¹ Alternatively, the all-holders/best price rule may be better extended to fully encompass the pre- and posttender offer periods.²⁷² Finally, withdrawal rights are arguably unnecessary in a world where their coercive aspect can be regulated by targets and where irrevocable tenders can provide bidders flagship support in unsolicited transactions.²⁷³ These are four further instances, but, in light of modern developments and the cobwebs set upon federal takeover regulation, the validity of the entirety of Williams Act regulation is subject to scrutiny and questioning.

B. *The Failure of Takeover Structure*

The Williams Act is not the only feature of federal takeover regulation that has failed to keep abreast with the progress of takeovers. Indeed, the shifting legal and structural landscape has arguably rendered obsolete the fundamental structure of federal takeover regulation.

269. The SEC rules on short and hedged tendering, in particular, have continually been controversial, at one point prompting a rare dissent by an SEC Commissioner in favor of deregulation. See Short Tendering Release, *supra* note 112, at 86,715-17. Short and hedged tendering can create a more efficient market in preacquisition shares and result in an arbitrage preclose price for a transaction that is closer to reality. This provides price and liquidity benefits to nontendering stockholders that arguably outweigh the loss to tendering stockholders who have fewer shares purchased. In light of the well-developed capital markets and arbitrage community present today it may be time to wholly deregulate short and hedged tendering.

270. For example, fairness opinions are increasingly controversial and SEC disclosure obligations on the subject increasingly inadequate—the impetus for pending NASD rules. See Steven M. Davidoff, *Fairness Opinions*, 55 AM. U. L. REV. 1557, 1595-98 (2006).

271. One commentator has cited the all-holders/best price rule as increasing the pressure to tender because “tendering shareholder[s] [are] assured of receiving the highest price that the bidder might offer.” Richard A. Booth, *The Problem with Federal Tender Offer Law*, 77 CAL. L. REV. 707, 713 (1989). Repeal of this rule would alter stockholder behavior and possibly relieve this pressure. In such a circumstance, any further needed protection could then come from acquiree and acquirer negotiation or through increased stockholder collective action.

272. The issue here is the possibility of further bidder purchases at a premium that are not shared equally with other target stockholders who, due to the inherent coercive nature of tender offers, may not tender early. This is the prisoner's dilemma. Their further disparate and uncoordinated nature does not permit them the ability to negotiate this right *ex ante*. But acquirees may negotiate this right in the face of a change in corporate control. See generally Subramanian, *supra* note 117, at 413 (proposing that stockholders “should replace their poison pills with a binding and enforceable agreement . . . to share any premium they receive in the context of a tender offer” in order to ensure sharing of any increased or lower back-end premium).

273. Unlimited withdrawal rights also hasten stockholder tenders by reducing the risk of early tendering. By incentivizing stockholders to tender early, they make unattractive bids look better and more likely to succeed. Booth, *supra* note 271, at 714.

1. Structural Incongruity

The stream of Delaware takeover decisions in the fourth and fifth waves has substantial implications for the structural focus of the federal takeover code. More specifically, the federal takeover code has traditionally had its locus in the Williams Act regulation of tender offers, with mergers regulated via the proxy rules. The SEC traditionally justified this distinction because mergers were viewed as being in lesser need of federal supervision. They were negotiated transactions between commercially sophisticated, reasonably equal parties; thus, the problematical, coercive aspects of tender offers were presumed absent.²⁷⁴ The initial federal regulatory focus upon tender offers was therefore appropriate since in the 1960s the aforementioned target defense was unavailable in the case of tender offers.

This preference also comported with unsolicited bidders' earlier penchant for tender offers over proxy contests.²⁷⁵ A tender offer is superior to a proxy contest since the bidder in a proxy contest must incur both the expense of the contest and the risk of complete defeat, whereas in a tender offer the bidder can condition its offer on the acquisition of a minimum number of shares which it can adjust as desirable. And historically, a bidder had a higher probability of success in a tender offer rather than a proxy contest due to "management's well-known dominance of the proxy machinery."²⁷⁶

The existence of the poison pill and other takeover defenses has rendered this federal regulatory bias moot. A proxy contest is now the only viable way for a bidder to acquire a recalcitrant target.²⁷⁷ The tender offer alone can no longer achieve corporate control in such situations. Yet Delaware law forcefully acts to favor targets over bidders in proxy contests to the possible detriment of stockholder choice. Delaware permits adoption of a staggered board.²⁷⁸ This arguably reduces the effectiveness of a proxy contest (and unsolicited bid), making it unappealing to anyone but the most persistent, and perhaps irrational, bidder.²⁷⁹ Similarly, Delaware notice and director removal statutes further impede

274. See Leebron, *supra* note 6, at 159-63 (discussing the structural relationship between the negotiated merger and the tender offer).

275. See *supra* notes 24-27 and accompanying text.

276. Fischel, *supra* note 246, at 7.

277. Recent successful examples of joint proxy contests and tender offers include BASF's successful bid for Englehard and Oracle's successful bid for Peoplesoft. See, e.g., Peter D. Lyons, *Unsolicited, But Welcome*, DAILY DEAL, July 25, 2006 (discussing BASF's tender offer and proxy solicitation); Steve Lohr & Laurie J. Flynn, *Oracle to Acquire Peoplesoft for \$10.3 Billion, Ending Bitter Fight*, N.Y. TIMES, Dec. 14, 2004, at C1 (discussing Oracle tender offer and proxy solicitation).

278. Corporations adopting a staggered board under Delaware law elect a fraction of their directors, usually one-third, each year to serve for a period of years, typically three. Thus, only a portion of the board can be replaced in any given year. See DEL. CODE ANN. tit. 8, § 141(d) (2006).

279. See generally Lucian Arye Bebchuk et al., *The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence, and Policy*, 54 STAN L. REV. 887 (2002) (finding empirical evidence that a staggered board has negative implications for corporate value). But see Mark Gordon, *Takeover Defenses Work. Is That Such a Bad Thing?*, 55 STAN L. REV. 819 (2002) (challenging the study of Bebchuk et al. and arguing that the staggered board provides benefits that outweigh its cost).

the timing and feasibility of these contests. They permit Delaware targets to confine proxy contests to a singular time of year, the annual election of the target board elections.²⁸⁰ This provides ample time for targets to anticipate and counteract looming bids. The likely consequence of these Delaware laws is to deter proxy contests, resulting in fewer bids and adverse effects on the value of potential acquirers.

The paradigm shift in unsolicited takeovers to proxy contests implicates the entirety of the federal takeover code, including the proxy and tender offer procedural and substantive rules. In a world where the poison pill is permitted continued existence, it militates towards deregulation of tender offers combined with increased regulation and oversight of proxy contests.²⁸¹ This appears particularly appropriate due to Delaware law's prejudice with respect to proxy contests. Yet on a microlevel, the SEC has not acted to revise or update the federal takeover rules to take this into account. Nor has the SEC considered the macro implications of this shift, including a changed regulatory focus and possible rulemaking action to restore a level playing field between bidders and targets in proxy contests for corporate control.

2. Structural Discrimination

Federal takeover law has traditionally distinguished in the scope and manner of its regulation of tender offers and mergers. However, the old, simplified reason for this distinction—the ability of a bidder to implement an unsolicited offer without target consent—is no longer valid. The death of the true hostile, functional requirement of target consent and other takeover developments has made many of these historical biases largely anomalous. More bluntly, there no longer appears to be any reason to continue the federal takeover code's general, disparate treatment of the two structures.

The most glaring example of this unwarranted discrimination is the undue timing advantage tender offers have over mergers. Tender offers currently have a minimum offer period of twenty business days; this compares with a two- to three-month minimum period to complete a merger.²⁸² Again, the justifications for this distinction appear no longer relevant in a world where acquiree consent is necessary, as the acquiree can negotiate its preferred takeover structure. One way to address this disconnect is to lengthen the tender offer period; perhaps an optimal result for the reasons discussed above. The other salve is obviously to shorten the merger period to bring it in line with the period for tender offers. This would require the SEC to revise Rule 14a-6 of the Exchange Act and for the SEC to reconsider its preclearance procedures for proxy statements before

280. See Grundfest, *supra* note 206, at 860 n.6 (citations omitted).

281. Even the Delaware courts have made this shift and now increasingly act to regulate proxy contests rather than tender offers. The reemergence of the *Blasius* line of review in *Liquid Audio* is perhaps the most powerful example. See *MM Cos. v. Liquid Audio, Inc.*, 813 A.2d 1118 (Del. 2003). But the willingness of the Delaware courts to forcefully apply *Unocal* in the proxy contest paradigm is another. See, e.g., *Omnicare, Inc. v. NCS Healthcare*, 818 A.2d 914 (Del. 2003); *Chesapeake Corp. v. Shore*, 771 A.2d 293 (Del. Ch. 2000).

282. See generally LOU R. KLING & EILEEN T. NUGENT, *NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES AND DIVISIONS* § 1.04[1][c][i] (2006).

mailing and solicitation of proxies.²⁸³ Depending upon the scope of revision it would also require the SEC to compel the stock exchanges to revise their own proxy solicitation regulation and preempt conflicting state laws.²⁸⁴ Ultimately, whatever the direction of the cure, the point is that the original timing distinction under federal law for these two structures no longer exist and appear inappropriate.

There are other cases where this discrimination no longer appears sustainable in light of a target's effective ability to control takeover structure. The federal disclosure requirements in mergers and tender offers are distinct, with variant and increased or lesser disclosure required for each.²⁸⁵ The propriety of this differentiation on the whole no longer seems apposite: full harmonization should be considered. Moreover, the all-holders/best price rule is applicable only to tender offers.²⁸⁶ There is no longer a reason for this. If the rule is maintained, application of the rule to merger transactions (or elimination in the case of tender offers) may be appropriate in order to stem the systematic bias that the rule, as currently interpreted, provides towards merger transaction.²⁸⁷ There is also the matter of bias under Rule 14e-5 discussed above.

283. Rule 14a-6 requires that unless otherwise agreed by the SEC, "preliminary copies of the proxy statement and form of proxy shall be filed with the Commission at least 10 calendar days prior to the date definitive copies of such material are first sent or given to security holders." 17 C.F.R. § 240.14a-6(a) (2006). The SEC will then decide whether to review and comment upon such proxy statement. The definitive proxy statement together with a proxy cannot be mailed until cleared by the SEC. While a 1992 rule change permits a preliminary proxy to be mailed so long as a proxy card is not included, no acquirer would in practice do so, due to the continuing possibility of SEC review and comment. *See generally* Bernard S. Black, *Next Steps in Proxy Reform*, 18 J. CORP. L. 1 (1992).

284. For example, Delaware requires that due notice of a stockholder meeting and accompanying proxy be mailed at least 20 days prior to the vote on a merger transaction. DEL. CODE ANN. tit. 8, § 251(c) (2006). Meanwhile, the NYSE recommends that a minimum of 30 days be allowed between the record and meeting dates. NYSE Listed Co. Manual § 401.03 (2006). Delaware also requires that the record date be no more than 60 nor less than 10 days before the date of such meeting. DEL. CODE ANN. tit. 8, § 213(a) (2006). This minut of time periods must be coordinated with any notice period for setting the record date as well as SEC timing restrictions.

285. A significant example is with fairness opinions. Federal securities law mandates disclosure of the analyses underlying a fairness opinion in a merger transaction but not a cash tender offer. There is no compelling reason for this disparity. *See* Davidoff, *supra* note 270, at 1590-94. There are also significant unwarranted timing distinctions in the delivery of information. In a cash tender offer transaction, information is typically published in the tender offer document within 5-10 business days. In a merger, however, there is no public disclosure until the definitive proxy statement is mailed to stockholders 1-2 months later.

286. 17 C.F.R. § 230.14d-10 (2006).

287. The application of the all-holders/best price rule to tender offers and not mergers has historically created prejudice towards use of the merger structure. *See generally* David Marcus, *Tender Returns*, DAILY DEAL, Jan. 30, 2006 (stating that acquirers have "increasingly opted to acquire targets by merger, where 14d-10 does not apply, rather than by tender offer"). The reason is that courts have broadly interpreted the meaning of a tender offer to arguably encompass change of control and other payments to executives in connection with the transaction. *See generally* Ben Walther, Note, *Employment Agreements and Tender Offers: Reforming the Problematic Treatment of Severance Plans Under Rule 14d-10*, 102 COLUM. L. REV. 774, 779-801 (2002) (outlining the divergent judicial opinions on the scope of Rule 14d-10 and its potential application to change-of-control compensation). But there has been no bright-line test announced for when these payments are so deemed in-

C. *The Failure to Regulate Takeovers*

Meanwhile, it is not just a matter of federal takeover laws that arguably have become obsolete. In the SEC's absence, a number of emergent and festering takeover issues remain unaddressed. These are areas of national import within the current regulatory purview of the SEC that the SEC has chosen through inaction not to regulate. I point out two of the more significant ones here.

1. *Change of Control Compensation*

Officers and other executive employees of an acquiree are often compensated in takeovers over and above the consideration paid to unaffiliated acquiree stockholders.²⁸⁸ The debate over this change of control compensation has been heated and prevalent. Some commentators have forcefully argued in favor of this compensation, asserting that it better aligns management and stockholder interests by shifting risk and incentivizing management to negotiate and accept takeover bids that might hurt their own pecuniary interests but otherwise benefit stockholders.²⁸⁹ Furthermore, in light of the ability for directors suborned by management to effectively block or impede takeovers, the need for this carrot is self-evident. The converse argument decries this compensation as a rent extrac-

cluded. Nonetheless, if a court makes this finding it will then order the acquirer to pay this differential compensation to all acquiree stockholders. This is a risk that an acquirer wishes to avoid—hence the historical bias towards mergers. *See generally* Michael D. Ebert, Comment, “*During the Tender Offer*” (or *Some Other Time Near It*): *Insider Transactions Under the All Holders/Best Price Rule*, 47 VILL. L. REV. 677 (2002); Jason K. Zachary, *Love Me Tender, Love Me True: Compensating Management and Shareholders Under the “All-Holders/Best-Price” Rule*, 31 SEC. REG. L.J. 81 (2003). The SEC recently adopted new regulations to address this issue. Amendments to the Tender Offer Best-Price Rules, Exchange Act Release No. 34-54684, [2006 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 87,511 (Nov. 1, 2006). But the ultimate regulations adopted by the SEC would still potentially act to prohibit this change of control compensation and preserve this bias. *See* Amendments to the Tender Offer Best-Price Rule, Exchange Act Release No. 52,968, [2005 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,772 (Dec. 23, 2005) (stating that “[w]e believe, however, that it would be inappropriate to limit the application of the best-price rule to a specific time frame”). The argument for not applying these rules to merger transaction is tenuous at best. Until the SEC applies this rule to both structures or cartails or repeals the scope of the rule, acquirers will still tend to favor merger transactions.

288. This benefit most commonly takes the form of “golden parachutes,” accelerated option vesting, and other compensation mechanisms which award executives upon a change in control of the corporation. The disproportionate gain can also take the form of employment or consulting arrangements, noncompetition agreements, or other future benefits provided by the acquirer to the acquiree’s management.

289. This benefit also serves as a compensatory mechanism: the change of control payments recompense for the manager’s lost investment of time and resources. There is also the base argument that they serve as a form of takeover defense. *See generally* Richard P. Bress, Note, *Golden Parachutes: Untangling the Ripcords*, 39 STAN. L. REV. 955, 955-63 (1987) (discussing the justification and structure of golden parachutes); Kenneth C. Johnsen, Comment, *Golden Parachutes and the Business Judgment Rule: Toward a Proper Standard of Review*, 94 YALE L.J. 909, 915-18 (1985). Another justification for these payments is that they reduce the corporation’s *ex ante* compensation costs, shifting them to a prospective acquirer and thereby increasing the value of the corporation if no takeover ever occurs. Alternatively, the compensation burden is shifted to an acquirer through a possible higher takeover premium. *See* Albert Choi, *Golden Parachute as a Compensation-Shifting Mechanism*, 20 J.L. ECON. & ORG. 170, 183-84 (2004).

tion, money pick-pocketed from unaffiliated stockholders. Officers are subject to fiduciary duties, and, accordingly, their duties should be to the stockholders; payment of this compensation is therefore wholly inappropriate and unnecessary. Moreover, these payments create a perverse incentive whereby the manager can be induced to drive down the acquiree share price in order to encourage a takeover.²⁹⁰ Change of control payments should therefore arguably be banned or subject to approval (precatory or otherwise) by stockholders.

The sums involved are numerically, if not relatively, large. A recent study of change of control payments to Chief Executive Officers (CEOs) found that CEOs, on average, accrue \$8 to \$12 million in change of control compensation triggered by a takeover.²⁹¹ This is an average—there are instances of much larger amounts. In 2005, James Kilts, CEO of Gillette, became entitled to \$165 million in change of control payments when Proctor & Gamble acquired Gillette.²⁹² In 2006, Bruce Hammonds, CEO of MBNA, accrued \$102 million in compensation when MBNA was acquired by Bank of America.²⁹³ Indeed, recent outcries over excessive executive pay include similar complaints about ubiquitous and inordinate change of control payments.²⁹⁴ The value of these payments has also become more suspect since a recent study found that when CEOs do receive extraordinary treatment through change of control compensation, the stockholders of the acquiree actually receive lower acquisition premia.²⁹⁵ The arguments that change of control payments are worthwhile since they reduce agency costs and ultimately benefit acquiree stockholders through a higher premium now appear less firm.

The SEC has not addressed this issue in any substantive manner, although it recently adopted increased disclosure requirements for change of control arrangements as part of an over-all review of executive compensation disclosure.²⁹⁶ Meanwhile, the Delaware courts and other potential regulators have refused to inject themselves into the debate concerning the appropriateness of these payments.²⁹⁷ The large sums involved, the public discontent, and the bias (or arguable benefit) that these payments potentially inject into the takeover

290. See generally Bress, *supra* note 289, at 961-62 (discussing criticism of golden parachutes); Johnson, *supra* note 289, at 918-23 (rejecting arguments that criticize golden parachutes and arguing that the benefits of these arrangements outweigh their costs).

291. Jay C. Hartzell et al., *What's in It for Me? CEOs Whose Firms Are Acquired*, 17 REV. OF FIN. STUD. 37, 39 (2004). See also Craig E. Lefanowicz et al., *Golden Parachutes and Managerial Incentives in Corporate Acquisitions: Evidence from the 1980s and 1990s*, 6 J. CORP. FIN. 215 (2000).

292. Gordon Platt, *Going for Gold*, GLOBAL FIN., Mar. 2006, at 18.

293. *Id.*

294. See, e.g., Ron Orol, *Those Parachutes: Just How Golden?*, DAILY DEAL, Jan. 18, 2006.

295. See Hartzell, *supra* note 291, at 39.

296. See Executive Compensation and Related Person Disclosure, Exchange Act Release No. 54,302, [2006 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 87,620 (Aug. 11, 2006).

297. The Delaware Supreme Court recently showed its bias against questioning these types of payments in the Disney case when it held that the payment of \$130 million severance package paid to Michael Ovitz did not constitute a breach of the board's fiduciary duties. See *In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27 (Del. 2006).

system make this an area that is clearly open for SEC investigation, study, and perhaps substantive or procedural rulemaking.

2. *Due Diligence and Disclosure*

Due diligence by prospective and actual acquirers is a murky and lightly regulated area raising three complex issues. The first is one of bidder equality. The U.K. Takeover Code requires that a prospective acquiree provide equal and prompt informational access to all prospective bidders.²⁹⁸ The federal takeover code has no such rule of equality or any other explicit rule governing bidder (prospective or otherwise) access to information. Consequently, acquirees can discriminate among bidders in the provision of information.²⁹⁹ This can lead to favoritism and reduced opportunities for competing, higher bids due to information inequality and asymmetry.

The second issue is one of stockholder equality. Regulation FD prohibits selective disclosure: generally speaking, when a corporation discloses material, nonpublic information it must make public disclosure of that information.³⁰⁰ However, Regulation FD does not apply to bidder due diligence.³⁰¹ Thus, a prospective bidder can obtain access to an acquiree's nonpublic information through the due diligence process. It can then decide, based on this information, whether to bid or not to bid. But if the bidder chooses not to bid, the nonpublic material information provided to the bidder is not required to be publicly disclosed. A prospective bidder therefore receives an informational advantage over ordinary stockholders who do not receive access to this material when making their own purchase decisions.

Finally, there is a third issue raised by acquirer receipt of acquiree information when the acquirer does decide to agree to a transaction. The disclosure requirements for acquirer due diligence in this circumstance are generally governed by the federal securities law antifraud strictures.³⁰² Beyond this, the SEC has not annunciated specific requirements for disclosure related to information supplied to acquirers by acquirees in the diligence process. Accordingly, the parameters of required disclosure are vague and acquirers tend to under-disclose

298. CITY CODE, *supra* note 259, at Rule 20.2.

299. This discrimination is permitted under Delaware law if the board has a reasonable belief that it will serve the interests of acquiree stockholders. *See, e.g., In re J.P. Stevens & Co., S'holders Litig.*, 542 A.2d 770, 781-83 (Del. Ch. 1988).

300. 17 C.F.R. §§ 243.100-.103 (2006).

301. Regulation FD by its terms does not apply to the extent the recipient agrees to maintain the disclosed information in confidence. *Id.* § 243.100. In addition, Regulation FD does not apply to any disclosure made in connection with a business combination involving the offering of securities registered under the Securities Act. *Id.* §§ 243.100-.102.

302. These rules generally prohibit material misstatements and omissions in connection with the purchase or sale of securities. Potentially applicable rules are section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b) (2000), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5 (2006) (general purchases and sales); section 14E of the Exchange Act and Regulation 14E thereunder, 15 U.S.C. § 78n(e) (2000) (tender offers) and Rule 14E thereunder, 17 C.F.R. § 240.14e-1 to -8 (2006); section 18 of the Exchange Act, 15 U.S.C. § 73f (2000) (documents filed with the SEC); Rule 13e-3(b)(1) under the Exchange Act, 17 C.F.R. § 243.13e-3(b)(1) (2006) (going-private transactions); and Rule 14a-9 under the Exchange Act, 17 C.F.R. § 243.14a-9 (2006) (proxy statements).

information received through the due diligence process. For example, projections relied upon by acquirers are often not disclosed or are disclosed in a summarized and rarely useful form.³⁰³ Contrast this with the U.K. rule which requires all assumptions underlying disclosed projections to be specifically stated and the policies and calculations supporting them to be examined and reported upon by the acquiree's accountants.³⁰⁴

Bidder due diligence, accordingly, raises a number of disclosure and equality issues that arguably adversely affect acquiree stockholders and the overall economic efficiency of the takeover process. Yet SEC regulation of, let alone attention to, these issues has been largely absent. This is mirrored in the state courts, which have also directed scant attention to the issues arising from bidder due diligence. Accordingly, further SEC examination and study of this area is appropriate and follow-up federal regulation should be considered.

D. *The Failure of Delaware*

Finally, there is the *deus ex machina*, the Delaware courts. Issues that were previously the concern of the SEC are now primarily, if not entirely, regulated by the Delaware courts.³⁰⁵ Delaware now acts alone in takeover standards and takeover defenses. Moreover, the positions of the Delaware court on these issues during the 1990s through today are markedly different than those of the fourth wave—an era of SEC engagement.

The modern-day takeover code engendered by this sea change is not necessarily the one that the SEC, had it been so engaged, would have fashioned or permitted. It is, of course, mere speculation to consider the type of regulation or other pressure that the SEC would have brought to bear, if any, on these issues as well as the effect any such *ex ante* influencing acts might have had on these Delaware court decisions. However, Delaware's current regulation of takeover defenses, at least, is largely contrary to the SEC's 1980s preferences.³⁰⁶ Similarly, in going-privates and transaction defenses, the Delaware courts have acted contrarily, or not at all, on issues of prior SEC focused concern.³⁰⁷

The Delaware courts have largely acted in all these areas to circumscribe stockholder protection and choice.³⁰⁸ This is a specific SEC interest in takeover regulation. Moreover, the Delaware-built takeover code is arguably adverse to

303. See, e.g., Guidant Corp., Definitive Proxy Statement (Form DEF14A), at 70 (Mar. 1, 2006) (noting exchange of projections but failing to disclose figures disclosed to acquirer); Gillette Co., Definitive Proxy Statement (Form DEF14A), at 41 (May 25, 2005) (noting exchange of projections but disclosing as material only projected growth rates for sales, profits from operations and earnings).

304. CITY CODE, *supra* note 259, at Rule 28.

305. The Delaware courts are also increasingly encroaching into the regulation of governing standards in takeover disclosure documents, previously the terrain of the SEC. See, e.g., Alessi v. Beracha, 849 A.2d 939 (Del. Ch. 2004) (denying motion to dismiss complaint premised on nondisclosure of takeover discussions); *In re Pure Resources, Inc. S'holders Litig.*, 808 A.2d 421 (Del. Ch. 2002) (holding analyses underlying fairness opinion required to be disclosed in tender offer documents despite lack of similar federal disclosure requirement).

306. See *supra* Part II.

307. See *supra* Part II.

308. See *supra* notes 230-36 and accompanying text.

other broader, national SEC interests. At a minimum, it is inapposite to the level-playing-field precepts embodied in Williams Act. Moreover, the Delaware takeover code discriminates to the preservation of management discretion.³⁰⁹ This is anathema to the SEC's historical goal of stockholder protection and autonomy.³¹⁰ This bias also fosters management entrenchment and exacerbates agency costs. This is inefficient and likely on the whole detrimental to the national economy.³¹¹

The SEC is therefore arguably obligated to shift the course and promulgate correcting regulation to the current Delaware-erected takeover code. This is not a question of federalism, the internal affairs doctrine, or whether the SEC should act beyond its current regulatory authority or even propose legislation to do so. The possibility of more sweeping action will be discussed in Part VI.C. Rather, this is a question similar to that posed when the SEC trumped Delaware's holding in *Unocal* on stockholder equality grounds by adopting the all-holders rule.³¹² Should the SEC fulfill its regulatory mandate, respond to and protect its constituencies and interests, and, in doing so, act to modify the takeover code promulgated by Delaware? The underlying premise here is that the national takeover code structured by the Delaware courts in the SEC absence is not an optimal one for the nation and is adverse not only to the congressional intent underlying federal securities regulation but also is contrary to the SEC's congressionally mandated role in the regulation of takeovers. If this is true, the federal takeover code is ripe for an update to cure these Delaware-induced deficiencies. In fact, the SEC is obligated to take such steps.

VI. A RETURN OF FEDERAL TAKEOVER REGULATION

A. A Reexamination of Federal Takeover Regulation

We have now seen that the consequence of the SEC absence is an obsolescent federal takeover code and suboptimal regulation of takeovers by the Dela-

309. See *supra* Part IV.

310. See *supra* note 167 and accompanying text.

311. There is a wealth of literature finding adverse economic effects resulting from the adoption of takeover and transaction defenses. See generally Bebchuk et al., *supra* note 279 (finding empirical evidence that adoption of a staggered board reduces stockholder wealth); P.R. Chandy et al., *The Shareholder Wealth Effects of the Pennsylvania Fourth Generation Anti-Takeover Law*, 32 AM. BUS. L.J. 399, 401 & n.14 (1995) (citing studies finding adverse economic effects surrounding the adoption of antitakeover devices); Coates & Subramanian, *supra* note 212, at 347 (finding empirical support for increased rates of takeover completion in the presence of lock-ups). But see John C. Coffee Jr., *The Uncertain Case for Takeover Reform: An Essay on Stockholders, Stakeholders and Bust-ups*, 1988 WIS. L. REV. 435, 437 n.7 (presenting a review of the conflicting conclusions of studies measuring the effect of the passage of stakeholder, or constituency, statute legislation); Lawrence D. Brown & Marcus L. Caylor, *Corporate Governance and Firm Performance* (2004) (citing empirical evidence to suggest that firms with antitakeover provisions, among other governance features, show greater returns over three-, five-, and ten-year periods than companies without comparable provisions), available at <http://www.issproxy.com/pdf/Corporate%20Governance%20Study%201.04.pdf>. See also Romano, *supra* note 135, at 113 (stating that state takeover statutes are "troublesome, for they can produce results that are inconsistent with the core goal of corporation law—the maximization of equity share prices").

312. See *supra* notes 151-53 and accompanying text.

ware courts. The magnitude of these deficiencies alone argues for more than tinkering; rather a wholesale reexamination of the federal takeover code. However, there are other reasons for such a step. First, the federal takeover code was largely erected through one-off, SEC rulemaking. The result is a patchwork quilt of a federal takeover code. It is time to examine the various interlocking pieces—how they work together as well as individually. Second, the wholesale shift in takeover law, structures, tactics and strategy require that the entire federal takeover code be attuned to these changes. Third, a takeover code is an interconditional and interdependent beast, and, as singular changes may implicate further revision, any reexamination of a rule should occur in the context of the whole.³¹³

There is also a trove of information and experience available to the SEC to inform such a reexamination; resources that were nonexistent when the SEC was last active. For example, the takeover systems outside the United States—Europe, Japan, and Australia, in particular—have substantially developed since the fourth wave and provide much experiential data.³¹⁴ Then there is the learning garnered from the United States.³¹⁵ Moreover, research in the takeover field has blossomed; pioneering studies of takeover defenses, transaction defenses, bidder and target tactics and strategies, other takeover rules as well as comparative work on takeover codes, and study of the structure of the takeover itself are now available.³¹⁶ The emergence of this constellation of resources also supports a reexamination of the federal takeover code.

This reexamination should not merely focus on restitching the frayed patchwork quilt. If there is a singular lesson to be learned from the takeover story of the past forty years, it is that takeover structures hurriedly evolve—more quickly than regulators, burdened by the rulemaking process, can respond. In order to forestall repeated obsolescence and the recurrence of piecemeal regulation, the SEC should consider formalizing the shadow principles which have previously guided its takeover rulemaking.³¹⁷ These include the principles of a

313. For example, if withdrawal rights are maintained, then elimination of Rule 14e-5 may be appropriate. If they are eliminated, then the original purpose for Rule 14e-5 is again present and Rule 14e-5 may still be necessary. See *supra* Part V.A.2.

314. For recent comparative review of these takeover codes, see generally CHRISTIN M. FORSTINGER, TAKEOVER LAW IN THE EU AND THE USA: A COMPARATIVE ANALYSIS (2002); Curtis J. Milhaupt, *In the Shadow of Delaware? The Rise of Hostile Takeovers in Japan*, 105 COLUM. L. REV. 2171 (2005); Geoffrey Miller, *Political Structure and Corporate Governance: Some Points of Contrast Between the United States and England*, 1998 COLUM. BUS. L. REV. 52; Paul von Nessen, *The Americanization of Australian Corporate Law*, 26 SYRACUSE J. INT'L L. & COM. 239, 259-62 (1999).

315. See *supra* Parts II-IV. See generally George Bittlingmayer, *The Market for Corporate Control (Including Takeovers)* (Mar. 18, 1998), available at <http://ssrn.com/abstract=81808>.

316. For a brief survey of these developments, see generally Gregg A. Jarrell et al., *The Market for Corporate Control: Empirical Evidence Since 1980*, 2 J. ECON. PERSP. 49 (1988); Michael C. Jensen & Donald H. Chew, *U.S. Corporate Governance: Lessons from the 1980s* (1995), available at <http://ssrn.com/abstract=146150>; Roberta Romano, *A Guide to Takeovers: Theory, Evidence, and Regulation*, 9 YALE J. ON REG. 119 (1992).

317. A principle-based takeover code would set forth the general principles underlying the takeover code. The regulator and participants would then act under the “spirit” of these principles and the detailed rules which would be promulgated thereunder to provide

level playing field *vis-à-vis* bidders and targets and the goal of stockholder protection and decisional primacy.³¹⁸ If the SEC adopts this course, it should enable it to respond more quickly to individual developments through application of principles rather than the several-year rulemaking process.³¹⁹ It will also have the virtue of dictating a logically coherent federal takeover code, one which has internal order to its promulgated rules.

Ultimately, though, the product of such review is not this Article's topic. I believe that such a review will bring to bear the SEC's national interests to conclude that the federal takeover code today is not right for the day.³²⁰ But it may not. The result will depend upon selection of first principles, the appropriateness of one-off regulation, perception of current deficits, the current scope of regulatory authority, political and interest group considerations and other vagaries of the regulatory process.³²¹ These make it difficult if not impossible to predict the exact outcome. However, without such a review we will not have the benefits of a systemwide reexamination, let alone a fix for any current dysfunction. The requirement and results of a review are therefore not outcome determinative to the extent the benefits of comprehensive analysis prevail.

Nor do I presume that such SEC reexamination will produce the results necessarily wanted by the SEC or otherwise generate unbiased, economically efficient regulation. The SEC rulemaking review and regulatory process is not a perfect one.³²² However, the SEC has historically maintained a sufficient dis-

specific direction. The principles would be articulated in open terms and therefore would be observed in both generalities and specifics. The U.K. Takeover Code is a model of one such code. See CITY CODE, *supra* note 259.

318. See *supra* note 167 and accompanying text. There are others, such as the one of equal opportunity, undergirding the all-holders/best price rules and the going-private rule. See John C. Coffee, Jr., *Transfers of Control and the Quest for Efficiency: Can Delaware Law Encourage Efficient Transactions While Chilling Inefficient Ones?*, 21 DEL. J. CORP. L. 359, 371-77 (1996). There is also the self-evident principle of the efficiency of the national capital markets. See 15 U.S.C. § 77b(b) (2000) (requiring that the SEC "consider, in addition to the protection of investors, whether the action will promote efficiency, competition and capital formation").

319. This could be implemented in part through a process that exists in the U.K. whereby participants regularly communicate with the Takeover Panel on issues of uncertainty.

320. Moreover, an important driver in this conclusion is that the bulk of the available studies show that takeover transactions are, in general, wealth-creating. See Ronald J. Gilson, *Lipton and Rowe's Apologia for Delaware: A Short Reply*, 27 DEL. J. CORP. L. 37, 40-48 (2002); Jensen & Chew, *supra* note 316, at 6-7; Roberta Romano, *supra* note 316, at 124 n.13. See generally Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110 (1965).

321. See generally Marc I. Steinberg, *The Securities and Exchange Commission's Administrative, Enforcement, and Legislative Programs and Policies—Their Influence on Corporate Internal Affairs*, 58 NOTRE DAME L. REV. 173 (1982) (discussing the various influences and process of SEC rulemaking).

322. However, the SEC is generally held in high esteem for its processes and output. See Robert A. Prentice, *The Inevitability of a Strong SEC*, 91 CORNELL L. REV. 775, 800 (2006) (stating that "most commentators consider the SEC an extremely successful regulator"); David L. Ratner, *The SEC at Sixty: A Reply to Professor Macey*, 16 CARDOZO L. REV. 1765, 1779 (1995) ("The SEC is one important reason why the securities industry is in so much better shape than other financial service industries, and why U.S. securities markets are the best securities markets in the world."). But see Langevoort, *supra* note 167, at 529

tance from industry and avoided capture, such that the chance of industry-biased regulation is low.³²³ The bias, if anything, is more towards inertia; however, when the SEC acts in takeovers it focuses on its own regulatory interests, its shadow principles.³²⁴ Therefore, from a historical perspective, action is the primary issue, not product.

There is still the question of congressional influence on any review and in the implementation thereof. Congress is capricious and acts within a wider political sphere.³²⁵ If the SEC revisions require legislation, such laws may not pass in the desired SEC form or even at all.³²⁶ Professor Roberto Romano, for example, has argued that congressional intervention and complete federalization of corporate law is undesirable since it is likely to produce more restrictive limitations on takeovers than those placed by the states.³²⁷

In order to stem these influences, the SEC should take steps to insulate any review from politics by channeling it through a specially appointed apolitical committee akin to the Advisory Committee. Moreover, congressional involvement can likely be forestalled through aggressive interpretation within the current regulatory framework. This has been a course the SEC has taken before with takeover regulation.³²⁸ Furthermore, more radical reform can also be implemented through SEC-mandated regulation via stock exchange rulemaking.³²⁹

(arguing that the SEC's takeover regulation is the result of organizational behavior concerned with internal self-serving goals); Jonathan R. Macey, *Administrative Agency Obsolescence and Interest Group Formation: A Case Study of the SEC at Sixty*, 15 CARDOZO L. REV. 909, 948 (1994) (concluding that "[t]he SEC's major litigation efforts and regulatory initiatives have been designed to protect the Commission's regulatory turf, rather than to further important areas of public policy"); A.C. Pritchard, *The SEC at 70: Time for Retirement?*, 80 NOTRE DAME L. REV. 1073, 1101 (2005) (arguing that the SEC is "independent" in name only and beholden to Congress such that "the SEC—under the watchful eye of Congress—has fueled the cyclical swings in regulatory policy as a means of gaining additional authority and budgetary support"). See generally ROBERTA S. KARMEL, *REGULATION BY PROSECUTION: THE SECURITIES AND EXCHANGE COMMISSION VS. CORPORATE AMERICA* (1982).

323. See SELIGMAN, *supra* note 16, at xix ("Few have suggested seriously that the SEC has been a 'captive' of the industries it regulates [S]uch a suggestion cannot be sustained by a reasonable reading of the Commission's history.")

324. See Stephen J. Choi & A.C. Pritchard, *Behavioral Economics and the SEC*, 56 STAN. L. REV. 1, 20-36 (2003).

325. See generally Roe, *supra* note 2, at 596-98.

326. This was the unfortunate case with the Sarbanes-Oxley Act. This legislation is seen by many commentators as rulemaking by Congress, over SEC objections, which produced inefficient and unproductive results. See Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 YALE L.J. 1521, 1595-97 (2005).

327. See Romano, *supra* note 101, at 503. See also Jonathan R. Macey, *Displacing Delaware: Can the Feds Do a Better Job than the States in Regulating Takeovers?*, 57 BUS. LAW. 1025 (2002); Mary E. Kostel, Note, *A Public Choice Perspective on the Debate over Federal Versus State Corporate Law*, 79 VA. L. REV. 2129, 2129 (1993) (arguing that "[t]he history and effects of the Williams Act suggest that federal regulation is unlikely to monitor better the behavior of corporate management in the gaps where the market for corporate control fails").

328. The adoption of the all-holders/best price rule, going-private rules, and rules requiring mandatory withdrawal rights through an offer period are prominent examples. See *supra* notes 56-70, 151-53 and accompanying text.

329. The SEC took this route in prohibiting midstream dual-class stock recapitalizations through stock exchange rulemaking after the SEC's own rule was struck down by the

In the end, the risk of a deficient or ham-fisted regulatory takeover code is certainly present. Yet this is counterbalanced by the deep flaws in the current regime and the consequent need for a wholesale reexamination and reform. The weight tips in this favor.

B. *The Return of the SEC*

Even if there is a wholesale update of the federal takeover code, the requirement of an active SEC within this context is a paramount goal in and of itself. The initial reason for this is practical; if the SEC does not tend to its takeover law, it will again quickly become outdated. Weeds grow in an uncared for lawn. This is true even if a principle-based takeover code is put forth, as specific enforcement, interpretation, and regulatory action under such rules remains necessary. Moreover, an active SEC will be better positioned to incorporate research and other practical experience as it unfolds.

An engaged SEC also provides positive force in a world where Delaware is now the primary takeover regulator. In the 1970s and 1980s takeover regulation was arguably an SEC game and many of the prostockholder decisions of the Delaware courts, including *Singer*, *Unocal*, and *Revlon* were arguably crafted in response to SEC pressure or the threat of SEC intervention.³³⁰ However, in the 1990s the evaporation of the SEC exigent pressure led the Delaware courts to veer sharply promanagement.³³¹

There is a lesson here. Throughout the contemporary history of takeovers, an active SEC has tempered the promanagement interests of Delaware. First, when Delaware or another state has leaned too far against federal interests, the SEC has acted to trump this conduct.³³² Second, the Delaware courts appear to be acutely aware of this real or potential federal action, and under this specter decide their cases in greater alignment with federal interests.³³³ This threat of active intercession tames Delaware's promanagement bias.³³⁴ The SEC presence alone is therefore a powerful mitigating device to ensure that the takeover code produced by the Delaware courts is one keyed to national needs.³³⁵

courts. *See generally* Bainbridge, *supra* note 117. *See also* Goldberg, *supra* note 241, at 235 (arguing for wholesale reform of the federal takeover code through "revision or imaginative application of section 14(e) of the Securities Exchange Act of 1934, or by adoption and enforcement by the stock exchange of effective self-regulatory rules").

330. *See supra* Parts II.B & II.C.

331. *See* Sean J. Griffith, *Daedalean Tinkering*, 104 MICH. L. REV. 1247, 1263 (2006) ("[W]hen the threat of federal preemption had faded . . . [c]ourts began to apply *Unocal* less aggressively and to narrow *Revlon* but, by retaining the principle of *intermediate* scrutiny, never to the point at which other states could steal incorporations by appealing to shareholders.").

332. This occurred in the case of first generation takeover statutes and the exclusionary self-tender. *See supra* notes 87, 132-34, 151-53 and accompanying text.

333. *See supra* notes 3, 236.

334. *See generally* Note, *The Case for Federal Threats in Corporate Governance*, 118 HARV. L. REV. 2726, 2726 (2005) (arguing that the "federal government threatening intervention [would] . . . prompt states to adopt more desirable rules").

335. *See* Roe, *supra* note 12, at 2502-04; *see also* McDonnell, *supra* note 12, at 136.

Concomitant to this point, the SEC is a national regulator. The SEC takes into account national interests rather than the narrow ones that Delaware acts upon.³³⁶ Historically, SEC regulation is likely to be prostockholder and in favor of rules that promote efficient national and international markets.³³⁷ Moreover, as Professor Roe has argued, the federal government can crush Delaware and represents a wider divergence of interests. If Delaware goes too far in representing its special interests to the detriment of those represented at the higher, federal level, the federal government will intervene.³³⁸ Compare this to Delaware's regulation which has tended towards rules that on their face favor manager decisional autonomy and entrenchment to the detriment of stockholders.³³⁹ Placed in a historical context, the SEC not only tempers Delaware but is more apt to enact a takeover code beneficial to the nation as a whole.

The SEC can also bring to bear capabilities as a national regulator that the Delaware courts or any other state regulator cannot. First, when the SEC acts, it acts nationally, and there is contiguity that no other state actor, even Delaware, can provide. Second, the SEC has the resources of the federal government at its disposal. The SEC can use these to support research, review developments, and continually study issues. It has superior personnel quality and numbers and consequently more capacity for enforcement action and regulation. Third, the SEC has a voice that speaks at a national level and with more focus and influence than any state actor.³⁴⁰

Finally, the SEC regulates in a manner wholly different than the nation's current takeover regulator, the Delaware courts. The SEC promulgates and enforces a rule-based takeover code, whereas Delaware regulates by court decision. There are benefits and deficits to both types of regulation. However, rule-based regulation is produced through a responsive deliberative process that involves a comment period and public input. It is consequently more nuanced, targeted, and globally consistent than regulation issued on a case-by-case basis.³⁴¹ It is not burdened by the Delaware courts' limitation of rulemaking based on the cases and underlying facts before it. In the instance of Delaware, this limitation is illustrated by the Delaware courts' tendency towards schizophrenic standards and haphazard enforcement.³⁴² While there are also arguments in favor of judicial takeover codes—they are arguably more flexible in responding

336. See Roe, *supra* note 12, at 2505-08.

337. This is confirmed by the historical discussion in Part II, *supra*.

338. Roe, *supra* note 12, at 2505-08.

339. See *supra* notes 230-36 and accompanying text. Delaware's interests include corporate managers who make the incorporation decision and the others in Delaware who benefit, the Delaware bar and its citizens. The stockholder interest is a diluted one since the choice for incorporation, the primary driver of Delaware's interests, is largely a management one. Delaware courts therefore arguably have an incentive to favor managers over stockholders. See Roe, *supra* note 12, at 2502-04.

340. See generally Prentice, *supra* note 322, at 801-03.

341. *Id.*

342. See generally Richard E. Kihlstrom & Michael L. Wachter, *Corporate Policy and the Coherence of Delaware Takeover Law*, 152 U. PA. L. REV. 523 (2003).

to changes in public mood, for example—a rule-based takeover code offers benefits that a case-based one inarguably cannot.³⁴³

Thus, there are clear national benefits to an active, engaged SEC. These benefits, however, do not mean that the ultimate product will be a beneficial and economic takeover code. This is due to an effect that countervailing forces, such as Congress and other federal bodies, may have on further, engaged regulation. It also may be due to internal workings or failures of the SEC. Yet an active SEC within the parameters of its rulemaking purview is what is being discussed here. This Article does not call for an engaged Congress—rather, an engaged SEC. While again there are risks of regulatory capture and misregulation, the history of the SEC's takeover regulation outlined in this Article leads one to conclude that it would take a measured approach to issues that arguably favored stockholders and national interests—as occurred in the 1960s through the 1980s.³⁴⁴ And, in the absence of scandal or public furor, Congress has largely left the SEC to regulate without interference.³⁴⁵ There is no reason to think this would be different in the future.

C. *Towards Refederalization?*

The return of the SEC as an active regulator and a wholesale update to federal takeover regulation leads to the natural question of whether this will result in the takeover code's complete federalization. This would rather be refederalization, since, as we have seen, takeovers prior to the mid-1970s were strictly a federal concern. Nonetheless, I do not think that this will occur or is appropriate for a number of reasons.

First, federalization would take congressional lawmaking. While incremental legislative and regulatory federalization is certainly possible and likely if this Article's call is successful, again, Congress is unlikely to approve wholesale federalization without some public outcry or scandal to motivate it.³⁴⁶ Thus practically, federalizing legislation is an outlier possibility that is unlikely to occur simply because of the reexamination and reengagement that this Article calls for.

Second, this Article is not a plea for or against federalization but for a cogent, comprehensive federal takeover code which takes into account national interests, is current, and is perpetuated in such manner. Again, some portion of the takeover code may be federalized as a result of SEC review and reengagement, but the focus should be on creating a functional national takeover code. In this regard, significant portions of the state code currently do regulate appropri-

343. For a discussion of the benefits of the Delaware system, particularly its ability to adjust to public developments, see Griffith & Steele, *supra* note 11, at 13-22.

344. See Steinberg, *supra* note 321 (outlining the positive role the SEC plays in national securities regulation).

345. See Banner, *supra* note 17, at 850 (observing that congressional action on securities regulation has largely been the product of scandal or other public furor).

346. See *id.* This is true even if the SEC acted through stock exchange rulemaking. The changes would likely be so significant that congressional approval would be an effective requirement.

ately and should be maintained.³⁴⁷ Moreover, a reengaged SEC would channel the state takeover code into a greater harmony with the SEC's desired national code. Any regulation by the SEC should take this into account. The issue is therefore one of an optimal takeover code, not federalization for its own sake.

Finally, federalization is arguably not an optimal norm on either a process or a substantive level. A judicially supervised takeover code can add value. The Delaware court process of case-by-case searching review is arguably not achievable through SEC regulation.³⁴⁸ Delaware fiduciary standards regulating the internal affairs of a corporation provide a base level of court supervision and regulation for takeovers that the SEC rules cannot.³⁴⁹ Thus, a vigorous duopoly appears to have potential to be a satisfactory regulator of takeovers. The preservation of Delaware would arguably mitigate risks of SEC industry capture as well as preserve an alternative laboratory for ideas and developments, albeit one subject to SEC supervision and response.³⁵⁰ It would also allow for quicker variances of response; either the SEC or the Delaware courts could act.³⁵¹ This is strong brew—a duopoly preserves the unique talents which each regulator can bring to bear.³⁵²

This is another lesson of the fourth wave. If each regulator focuses on its interests, it can arguably build a more fitting, politically and economically optimal takeover code.³⁵³ This appeared to be the destination of takeover regulation in 1985, the year of the Delaware court's decisions in *Revlon* and *Unocal* and a high tide for SEC involvement. Alas, the dream went by the wayside upon the SEC's subsequent withdrawal. Nonetheless, SEC regulation should take this collaboration into account to craft a national code which maintains space for state takeover regulation. The SEC will obviously maintain a check on Delaware and the other states, but this trump should be one utilized only when national interests militate.

347. See Griffith & Steele, *supra* note 11 (arguing the benefits of the Delaware corporate code).

348. See Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009 (1997) (discussing the unique style of the Delaware courts' writings).

349. See Gilson, *supra* note 320, at 40-42 (2002) ("Courts cannot distinguish with precision whether underperformance results from bad luck on the one hand, or bad judgment on the other. The business judgment rule properly serves to allocate that assessment to the market."); Ehud Kamar, *A Regulatory Competition Theory of Indeterminacy in Corporate Law*, 98 COLUM. L. REV. 1908, 1939 (1998) (arguing that "[t]he competitive advantage that Delaware derives from legal indeterminacy may have shaped its law indirectly").

350. See Marcel Kahan & Edward Rock, *Symbiotic Federalism and the Structure of Corporate Law*, 58 VAND. L. REV. 1573, 1576 (2005).

351. This is a natural outcome of having two focused regulators, although of course conflicting regulation is also a possibility. The trump available to the SEC, however, should alleviate and forestall this problem.

352. *Cf.* Kamar, *supra* note 349 (arguing for imperfect competition of suboptimal regulation as a plausible intermediate regulatory structure between perfect competition and monopoly).

353. This would be accomplished through the threat and actuality of SEC intervention if harmonized regulation was not achieved.

VII. CONCLUSION

Our whirlwind tour of federal takeover regulation has exploded a surrounding myth. The myth was that of the SEC as a currently active regulator of takeovers. This was once fact; the SEC was the primary regulator of takeovers from the 1960s through to the twilight of the 1980s. But it is no longer the case; since 1989 the SEC has largely abstained from the regulation of takeovers.

The consequences of this truth are manifold. In the SEC absence, federal takeover law has become obsolete. It oftentimes regulates incongruously, does not regulate important areas, or regulates in a manner inconsistent with the welfare of its interested parties. Moreover, the SEC's failure to tend the federal takeover code and practice of one-off rulemaking has created incoherence. Many takeover rules now lack justification or otherwise do not function effectively in tandem with the remaining federal code. In short, there is an existing failure of federal takeover regulation.

The post-1989 abstention of the SEC has also resulted in the emergence of the Delaware courts as the nation's primary takeover regulator. Delaware has vigorously seized this position and proceeded to erect a takeover code structured in accordance with its narrow pro-management and other self-interests. The consequence is a suboptimal takeover code, one that is contrary to national interests as well as the SEC's traditional concerns of stockholder protection and decisional autonomy.

This all sustains a loud cry for an SEC reexamination and update of the federal takeover law, and for the SEC's return as an active, engaged regulator of public takeovers. The result would not only be a forward-going, current takeover code, but one that keeps the Delaware courts in check. This would engender a more economically efficient, informed, and internally ordered national takeover code in the better interests of stockholders and the nation.