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The Proper Relationship Between Federal and State Law in the Regulation of Tender Offers

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The Proper Relationship Between Federal and State Law in the Regulation of Tender Offers

William C. Tyson*

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INTRODUCTION

Prior to 1960, cash tender offers¹ were virtually nonexistent in the United States.² In the period of business growth that followed, however, they gained an aura of respectability and came into vogue as a method of corporate acquisition.³ During this period, the dearth of meaningful federal regulation of the cash tender offer process⁴ stood in sharp contrast to the long-standing

1 In general, cash tender offers are publicized requests made to shareholders of one company for tenders of their securities at a fixed cash price. See *infra* note 56.

2 Only eight cash tender offers were made before 1960. The aggregate amount of those offers totaled less than two hundred million dollars. In 1966, however, there were over one hundred cash tender offers which, in the aggregate, totaled almost one billion dollars. H.R. REP. NO. 1711, 90th Cong., 2d Sess. 2 (1968), reprinted in 1968 U.S. CODE CONG. & ADMIN. NEWS 2811, 2812.

3 See E. ARANOW & H. EINHORN, TENDER OFFERS FOR CORPORATE CONTROL 65-66 (1973) (discussing nine factors that were responsible for the proliferation of cash tender offers in the 1960s); see also L. LOSS, FUNDAMENTALS OF SECURITIES REGULATION 497-99 (2d ed. 1988) (suggesting that Americans copied the British "takeover bids").

4 Exchange tender offers—requests made to shareholders of one company for tenders of their securities in exchange for securities of the acquiring company—did occur

and elaborate federal regulation of the proxy campaign, which was the traditional method of capturing corporate control.⁵ Indeed, the federal scheme for proxy regulation harkened back to the proxy rulemaking power Congress gave to the Securities and Exchange Commission (SEC) in the Securities Exchange Act of 1934 (Exchange Act).⁶ By the 1960s, federal regulation consisted of a detailed set of rules governing the entire proxy machinery.⁷ Then in 1968, Congress closed the regulatory gap by adopting the Williams Act,⁸ which amended the Exchange Act.⁹ The Williams Act, which was modeled in several respects after the proxy rules,¹⁰ instituted a comprehensive regulatory scheme for both cash tender offers and substantial acquisitions of securities.¹¹

prior to the 1960s, and they were subject to the registration requirements of the Securities Act of 1933 (Securities Act), 15 U.S.C. §§ 77a-77aa (1988). See L. LOSS, *supra* note 3, at 498. Mergers are not tender offers.

5 See H.R. REP. NO. 1711, *supra* note 2, at 2-4, reprinted in 1968 U.S. CODE CONG. & ADMIN. NEWS at 2812-13; S. REP. NO. 550, 90th Cong., 1st Sess. 2-4 (1967); L. LOSS, *supra* note 3, at 498 (stating that "there was no federal regulation remotely comparable to the proxy rules"); Sowards & Mofsky, *Corporate Take-Over Bids: Gap in Federal Securities Regulation*, 41 ST. JOHN'S L. REV. 499, 501-02 (1967).

6 15 U.S.C. § 78n(a) (1988) (original version at ch. 404. tit., I, § 14, 48 Stat. 881 (1934)). Congress prohibited the solicitation of proxies (in respect of certain securities) in contravention of rules that the SEC "may prescribe as necessary or appropriate in the public interest or for the protection of investors." *Id.*

7 See 17 C.F.R. § 240.14a-1 to -14, -101 (sched. 14A), -102 (sched. 14B) (1990) (version that was current in the 1960s at 17 C.F.R. § 240.14a-1 to -12, -101, -102 (1967)). Proxy regulation is also based on 15 U.S.C. § 78n(b)-(c) (1988), and the SEC rules thereunder, 17 C.F.R. § 240.14b-1, .14b-2, .14c-1 to .14c-7, .14c-101 (sched. 14C) (1990).

8 Pub. L. No. 90-439, 82 Stat. 454 (1968) (codified as amended at 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1988)).

9 The Williams Act added § 13(d)-(e) and § 14(d)-(f) to the Exchange Act, 15 U.S.C. §§ 78a-78ll (1988).

10 Congress was aware of the parallel between proxy contests and tender offers. See *Full Disclosure of Corporate Equity Ownership in Corporate Takeover Bids: Hearings on S. 510 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. 206 (1967) [hereinafter *Senate Hearings*]. SEC Chairman Manuel Cohen explained that "[t]he procedures provided by the bill in the case of contested tender offers are analogous to those now followed when contending factions solicit proxies under the Commission's proxy rules." *Id.* at 20-21. Note that three of the tender offer provisions of the Williams Act were incorporated into § 14 of the Exchange Act, the section governing proxies. Two commentators have argued that Congress' effort to model the tender offer disclosure requirements after those applicable to proxy statements was unwise because shareholders involved in a tender offer do not have the opportunity to utilize the information disclosed. Jordan & Woodward, *An Appraisal of Disclosure Requirements in Contests for Corporate Control*, 46 GEO. WASH. L. REV. 817, 843 (1978).

11 Sections 14(d) and 14(e) regulate tender offers, § 13(d) regulates substantial acquisitions of securities, and § 13(e) and § 14(f) regulate both tender offers and substantial acquisitions.

The overriding objective of the Williams Act was to provide evenhanded protection to all participants in the tender offer process. In particular, the Act sought to ensure that shareholders of the target company had the information and time necessary to consider an offer, that shareholders were treated fairly, and that a competitive balance was maintained between the tender offeror and the target company.¹² To further these statutory goals, Congress adopted a broad antifraud/antimanipulation provision explicitly addressed to the tender offer context¹³ and granted the SEC specific rulemaking authority,¹⁴ which the SEC has used extensively.

The Supreme Court has decided three cases under the tender offer provisions of the Williams Act at the time of this writing: *Piper v. Chris-Craft Industries*¹⁵ in 1977, *Schreiber v. Burlington Northern, Inc.*¹⁶ in 1985, and *CTS Corp. v. Dynamics Corp. of America*¹⁷ in 1987. In each case, the Court interpreted the legislation restrictively, denying private parties rights or remedies claimed to derive from the statute.¹⁸ These three decisions have had immense impact on corporate takeovers. By consistently embracing a restrictive interpretation of the Williams Act, the Court has paved the way for an increasing paramountcy of state law in the regulation of tender offers. Furthermore, because proxy regulation has remained primarily a matter of federal law, the entrance of state law into tender offer regulation has created a dichotomy in the

12 For a discussion of the goals and provisions of the Williams Act, see *infra* text accompanying notes 53-109.

13 15 U.S.C. § 78n(e) (1988).

14 *Id.* §§ 78m(d)(1)-(2), 78m(d)(5)-(6), 78m(e)(1)-(2), 78n(d)(1), 78n(d)(4)-(5), 78n(d)(8), 78n(e)-(f).

15 430 U.S. 1 (1977).

16 472 U.S. 1 (1985).

17 481 U.S. 69 (1987).

18 The Supreme Court has interpreted the Williams Act in one other case, *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49 (1975). However, *Rondeau*, which was the Court's first Williams Act decision, did not involve the tender-offer provisions of the Act, but rather involved § 13(d) of the Act. In *Rondeau*, a target company sued a purchaser for failing to file timely reports as required by § 13(d). The target sought a permanent injunction prohibiting the acquisition of additional shares, and the issue before the Court was whether the target had to demonstrate irreparable harm in order to secure the requested injunctive relief. The Court held that irreparable harm must be demonstrated and found that since only a technical, unintended violation of the Act had occurred, relief should not be granted. *Id.* at 58-59, 65. Thus, by adopting a restrictive approach to the remedial aspects of the Act, *Rondeau* is consistent with the three tender offer cases that were to follow. Chief Justice Burger delivered the opinion in *Rondeau* and was joined by Justices Stewart, White, Blackmun, Powell, and Rehnquist. Justices Douglas, Brennan, and Marshall dissented.

regulation of the two methods of capturing control of an unwilling target. The story how all of this happened tempts the pen!

Before the passage of the Williams Act, the Supreme Court, in 1964, rendered a landmark decision under the proxy rules which signalled that the rules were to be construed liberally and expansively. In *J.I. Case Co. v. Borak*,¹⁹ the Court held that a private party had standing to maintain an implied cause of action for violations of the proxy antifraud rule. Keenly aware that neither the rule nor the statutory provision under which the rule was adopted expressly permitted private lawsuits, the Court nonetheless created, by judicial interpretation, a federal implied right of action for damages and rescission. The Court realized that without such a private remedy, victims of deceptive proxy statements would be relegated to state law for remedial relief.²⁰ *Borak*, which was the first Supreme Court decision to imply a private right of action under any federal securities statute,²¹ naturally had a substantial effect on proxy battles—each side of the contest was almost assured a federal cause of action if the other side violated the rules.

Borak also served as a guidepost, at least initially, for the federal courts that were called upon to apply the new tender offer law, which, like the proxy rules, did not contain express liability provisions. Indeed, during the early years of the Williams Act's life, the lower federal courts granted virtually every participant in the tender offer process standing to sue for violations of the Act.²² Then in 1977, in *Piper*, the Supreme Court denied an unsuccessful tender offeror standing to sue a competing offeror and target management for damages under the antifraud provision of the Williams Act.²³ Although the Court was careful to limit its holding to damage suits brought by a tender offeror under the antifraud provision,²⁴ federal courts have read *Piper* as a general limitation on the standing of both offerors and targets to sue for damages under all provisions of the Williams Act. Some courts have questioned the propriety of equitable relief as well.²⁵ As a result, reliance on state law is often the only alternative for

19 377 U.S. 426 (1964).

20 *Id.* at 434.

21 See L. LOSS, *supra* note 3, at 926-27.

22 See cases cited *infra* note 139.

23 *Piper*, 430 U.S. at 42.

24 *Id.* at 42 n.28.

25 See *infra* notes 205-07 and accompanying text.

parties aggrieved by violations of the Act. The *Piper* Court, however, specifically distinguished and preserved its holding in *Borak*.²⁶ Thus, for over a decade, there has been a disparity in the remedial aspects of the proxy rules and the Williams Act that glows with an incandescent illogic: two-way standing and federal law for proxy violations, but often no standing and state law for tender offer violations.

In 1985, in *Schreiber*, a target shareholder—the one tender offer participant that seems to have survived *Piper* with the right to sue under the Williams Act—brought suit against a tender offeror, the target, and the directors of the target for damages, alleging that they had engaged in manipulative tender offer practices within the meaning of the antimanipulation provision of the Act.²⁷ Specifically, the shareholder claimed that the offeror's revocation of a hostile tender offer coupled with the substitution of a friendly tender offer (after negotiations with target management) was a manipulative distortion of the market for the target stock that resulted in a diminished payment in the second offer to those shareholders who had tendered during the first offer. The defendants' conduct was not accompanied by any misrepresentation, and the conduct was completely disclosed.²⁸ The Supreme Court rejected the shareholder's claim, holding that tender offer practices were not manipulative unless there was some sort of misrepresentation or nondisclosure.²⁹ Any claim the shareholder may have had for breach of fiduciary duty or breach of contract was left to be addressed in a state forum. As might be expected, the Court's restrictive interpretation of tender offer manipulation in *Schreiber* had import that extended well beyond the facts of the case; it made nondeceptive but unfair tender offer conduct exclusively a question of state corporation law by foreclosing challenges under federal law, and it raised serious questions about the validity of several SEC rules that seek to prevent this type of tender offer conduct.

Just as *Piper* and *Schreiber* laid the groundwork for a growing prominence of state *judicial* regulation of the tender offer process, *CTS* in 1987 countenanced state *legislative* regulation. The events that led up to this third visit from the Supreme Court span a twenty-year period and are best described chronologically.

26 *Pipers*, 430 U.S. at 41.

27 *Schreiber*, 472 U.S. at 4.

28 *Id.* at 12-13.

29 *Id.* at 12.

Although the states have never attempted to pass legislation regulating proxy contests,³⁰ in the ten-year period after the Williams Act was adopted, approximately three-quarters of the states enacted tender offer legislation, and this legislation gave target companies more protection than the federal statute.³¹ In general, these statutes had extraterritorial application, imposed a precommencement waiting period, and gave the state government the power to pass on the merits of the offer. The proliferation of these so-called first-generation state takeover statutes gave rise to a considerable number of constitutional attacks in both federal and state courts, and most of the courts ruled that the statutes at issue were unconstitutional, both under the commerce clause as substantially interfering with interstate commerce and under the supremacy clause as being in conflict with the Williams Act. Then in 1982, in *Edgar v. MITE Corp.*,³² the Supreme Court held that the Illinois statute was unconstitutional on commerce clause grounds,³³ and a plurality of the Court argued that the statute was preempted by the Williams Act.³⁴ Although *MITE* had the effect of invalidating all remaining state takeover legislation, it embodied guidelines that the state legislatures could follow if they wished to adopt new takeover laws that avoided the constitutional infirmities of the Illinois statute.

Predictably, after *MITE*, a second generation of state takeover statutes soon emerged.³⁵ These statutes narrowed the bases for asserting jurisdiction and were couched as substantive state regulation of corporate governance, utilizing traditional areas of state corporation law such as shareholder voting rights or mergers. They were of various types, but an exemplar is the control share acquisition law. Under this type of statute, once a tender offeror has acquired a specified percentage of shares in the target company, a majority of the disinterested target shareholders must agree to give the offeror the right to vote its shares. In *CTS*, the Supreme Court tested the constitutionality of a control share acquisi-

30 L. Loss, *supra* note 3, at 449 n.1.

31 For a discussion of this first round of state takeover legislation and the constitutional challenges that were made, see *infra* text accompanying notes 386-402.

32 457 U.S. 624 (1982).

33 *Id.* at 646.

34 *Id.* at 629. The majority opinion did not address the Williams Act or the preemption issue. For a discussion of the plurality opinion in *MITE*, see *infra* text accompanying notes 403-14.

35 For a discussion of the second-generation takeover statutes and the constitutional challenges that were made, see *infra* text accompanying notes 415-24.

tion statute adopted in Indiana. The Court held that the Indiana statute was a legitimate exercise of state authority and found that it neither interfered with interstate commerce nor conflicted with the Williams Act.³⁶ *CTS* resulted in a new wave of state statutes, often on the Indiana model.³⁷ This legislation, now more constitutionally secure, added another asymmetry to proxy and tender offer regulation only federal legislation applied in the proxy area, but both federal and state legislation applied to tender offers.

The Congress of 1968 would be unsettled by this story of the development of tender offer law, because, as this Article argues, the Supreme Court has emasculated the Williams Act by a faulty construction of the Act's provisions and purposes and, as a result, has derailed tender offer regulation from the federal track Congress intended. The Article maintains that by deferring to state common-law remedies in *Piper*, by bowing to state corporation law in *Schreiber*, and by approving state legislative strategies in *CTS*, the Court has adopted a philosophy of federalism which is so vigilant in safeguarding the rights and powers of the states that state law has been allowed to disturb the federal design for the regulation of tender offers. The Article also maintains that if today's lawmakers evaluated the federal design Congress envisioned when it passed the Williams Act, they would find that this design is as desirable today as it was in 1968. The Article therefore concludes that Congress should infuse renewed potency into the Act by nullifying the Court's trilogy of tender offer cases. Such action, the Article observes, would put tender offers and proxy contests on an equal footing from a regulatory standpoint and thus make the regulation of corporate takeover battles primarily the domain of federal law.

Organizationally, Part I of the Article summarizes the legislative history, objectives, and pertinent provisions of the Williams Act. Part II criticizes *Piper* and argues that Congress wanted all tender offer participants to have standing to sue under the Williams Act. Part III evaluates *Schreiber* and maintains that the Williams Act was meant to prohibit certain nondeceptive but unfair tender offer practices. The impact of *Schreiber* on targets' defensive tactics, on bidders' offensive strategies, and on the SEC's tender offer rules is also analyzed. Part IV criticizes *CTS* and ar-

36 *CTS*, 481 U.S. at 86-87, 94.

37 For a discussion of state takeover legislation after *CTS*, see *infra* text accompanying notes 470-500 .

gues that the major types of state takeover statutes currently in force are preempted by the Williams Act. Finally, Part V discusses the Article's conclusion that Congress should negate *Piper*, *Schreiber*, and *CTS* with legislation that gives unquestioned primacy to federal law in the regulation of tender offers. Specific recommendations for this needed congressional action are then set forth.

I. THE WILLIAMS ACT

A. Legislative History and Statutory Objectives

The dramatic increase in the number of cash tender offers in the 1960s created a large gap in the federal securities laws.³⁸ Tender offerors were able to operate in almost complete secrecy with no obligation to disclose information to shareholders of the target company when making a bid.³⁹ Moreover, target share-

38 Unlike exchange tender offers (*see supra* note 4), cash tender offers were not subject to the registration requirements of the Securities Act. *See* H.R. REP. NO. 1711, *supra* note 2, at 3, *reprinted in* 1968 U.S. CODE CONG. & ADMIN. NEWS at 2812-13; S. REP. NO. 550, *supra* note 5, at 2-3; Bromberg, *The Securities Law of Tender Offers*, 15 N.Y.L.F. 462, 463 (1969); Hamilton, *Some Reflections on Cash Tender Offer Legislation*, 15 N.Y.L.F. 269, 273-75 (1969); Hayes & Taussig, *Tactics of Cash Takeover Bids*, 45 HARV. BUS. REV. 135, 137 (1967). As a result, the only provisions of the federal securities laws that had any potential application to the cash tender offer process were the insider trading provisions of rule 10b-5, 17 C.F.R. § 240.10b-5 (1990), and § 16 of the Exchange Act, 15 U.S.C. § 78p (1988). *See* L. LOSS, *supra* note 3, at 498. State law was not much better than federal law. Only one state, Virginia, had enacted a takeover statute at the time the Williams Act was adopted, and that statute had been on the books for only four months. *See* Take-Over-Bid Disclosure Act, ch. 119, 1968 Va. Acts 167 (repealed 1989). And at common law, majority shareholders selling a controlling block had been held liable to the corporation or minority shareholders but only when they had reason to believe that the purchaser was likely to mismanage the corporation or loot it. *See, e.g.,* Perlman v. Feldman, 219 F.2d 173 (2d Cir.), *cert. denied*, 349 U.S. 952 (1955); *Insuranceshares Corp. v. Northern Fiscal Corp.*, 35 F. Supp. 22 (E.D. Pa. 1940); *Gerdes v. Reynolds*, 28 N.Y.S.2d 622 (Sup. Ct. 1944). *See generally* Andrews, *The Stockholder's Right to an Equal Opportunity in the Sale of Shares*, 78 HARV. L. REV. 505 (1965); Bayne, *A Philosophy of Corporate Control*, 112 U. PA. L. REV. 22 (1963); Hill, *The Sale of Controlling Shares*, 70 HARV. L. REV. 986 (1957); Jennings, *Trading in Corporate Control*, 44 CALIF. L. REV. 1 (1956); Leech, *Transactions in Corporate Control*, 104 U. PA. L. REV. 725 (1956). In addition, parties seeking to thwart a tender offer could have been held liable at common law for the tort of interference with a prospective advantage. *See* W. KEETON, D. DOBBS, R. KEETON & D. OWEN, PROSSER AND KEETON ON TORTS § 130, at 1005-31 (5th ed. 1984); *infra* notes 208 & 210; *see also* Fleischer & Mundheim, *Corporate Acquisition by Tender Offer*, 115 U. PA. L. REV. 317, 356 n.150 (1967). Common-law tort actions, however, were extremely limited and, at bottom, did not provide a viable remedy for intentional misconduct in the tender offer context. *See, e.g.,* *Middlesex Concrete Prod. & Excavating Corp. v. Carteret Indus. Ass'n*, 37 N.J. 507, 518-19, 181 A.2d 774, 781 (1962).

39 The offeror was under no obligation to disclose its identity, the source of its

holders were often forced to act hastily on offers before target management or other groups had an opportunity to present opposing arguments or competing offers.⁴⁰ Finally, the various participants in the tender offer process, as part of their offensive or defensive strategies, were able to engage, frequently with impunity, in numerous deceptive and manipulative practices.⁴¹

Convinced that the regulatory gap should be filled and that some of the abusive tender offer practices that had arisen should be curbed, in 1965 Senator Harrison Williams introduced Senate Bill 2731.⁴² The bill, an avowedly promanagement proposal,⁴³ imposed precommencement disclosure requirements on tender offerors and purchasers of substantial blocks of a company's securities.⁴⁴ No action was taken on the bill,⁴⁵ but it was revised with the assistance of the SEC and reintroduced by Senator Williams in 1967⁴⁶ as Senate Bill 510.⁴⁷

funds, its associates, or its future plans if control were obtained. H.R. REP. NO. 1711, *supra* note 2, at 3, *reprinted in* 1968 U.S. CODE CONG. & ADMIN. NEWS at 2812-13. Senator Thomas Kuchel deplored the "tragedy" of the "rape" of corporations by raiders acting under a "cloak of secrecy." *Senate Hearings, supra* note 10, at 43.

40 The offeror was under no obligation to give target shareholders any specified time to consider the offer, and often the offers were made under conditions suggesting that a "hasty deposit" was necessary because the transaction would be conducted on a "first[-]come, first[-]serve[d]" basis. *Senate Hearings, supra* note 10, at 17; H.R. REP. NO. 1711, *supra* note 2, at 3, *reprinted in* 1968 U.S. CODE CONG. & ADMIN. NEWS at 2812-13. Pressure tactics were also used by target management to lull shareholders into "refusing a tender offer on the basis of unsubstantiated or irrelevant arguments." *Senate Hearings, supra* note 10, at 204-05.

41 *See Senate Hearings, supra* note 10, at 60, 62, 196, 236.

42 S. 2731, 89th Cong., 1st Sess. § 2 (1965); *see* 111 CONG. REC. 28,257-60 (1965).

43 Senate Bill 2731 had a somewhat limited objective and has been aptly characterized as the "Incumbent Management Protection Act." *See Moylan, Exploring the Tender Offer Provisions of the Federal Securities Laws*, 43 GEO. WASH. L. REV. 551, 553 (1975).

44 The bill required that "any cash tender offers and, indeed, any substantial accumulation of shares . . . be preceded by the filing of public information." 111 CONG. REC. 28,259 (1965). Senator Williams saw such disclosure as "the only way that corporations, their stockholders, and employees [could] be adequately prepared in advance to meet the threat of the takeover specialist." *Id.* That Senator Williams envisioned the threat as an ominous one is evidenced by his remarks when introducing the bill: "In recent years we have seen proud old companies reduced to corporate shells after white-collar pirates have seized control with funds from sources which are unknown in many cases, then sold or traded away the best assets, later to split up most of the loot among themselves . . ." *Id.* at 28,257.

45 E. ARANOW & H. EINHORN, *supra* note 3, at 66.

46 *See* 113 CONG. REC. 854-57, 24,662-64 (1967); 112 CONG. REC. 19,003-07 (1966).

47 S. 510, 90th Cong. 1st Sess. (1967). The bill was co-sponsored by Senator Kuchel and had the approval of virtually all the major stock exchanges. *See* 113 CONG. REC. 24,665 (1967).

The new bill reflected a shift in attitude. Although still committed to the principle of disclosure of information, Congress realized in the interim period that tender offers provided a useful check on inefficient, entrenched management, and that therefore any bias in the legislation in favor of target management was not wise because it might prevent some offers from ever being made.⁴⁸ As a result, in revising Senate Bill 2731, Senator Williams followed the SEC's suggestion that the administrative approach of neutrality in the regulation of proxy contests—an approach firmly grounded on the Exchange Act's legislative history⁴⁹—would also be appropriate for tender offer regulation.⁵⁰ Hence, instead of the promanagement approach taken in Senate Bill 2731, Senate Bill 510 embraced a policy of neutrality, which was accomplished by imposing restrictions on the conduct of target management and others who opposed the tender offer and by reducing the constraints on the conduct of the tender offeror.⁵¹

48 S. REP. NO. 550, *supra* note 5, at 3. Congress also was convinced that tender offers fostered competitive bidding for target stock, thus affording target shareholders the opportunity to tender their shares at a premium. 113 CONG. REC. 24,666 (1967) (remarks of Sen. Javits). Furthermore, Congress believed that a promanagement bill, even if it did not prevent some offers from ever being made, would give management a decided advantage by precluding a fair and free flow of information to target shareholders from offerors and management alike, to the detriment of target shareholders. *See* Edgar v. MITE Corp., 457 U.S. 624, 635 (1982) (plurality opinion) (suggesting that the advance disclosure requirements of S. 2731, which would have had the effect of allowing a target company to disseminate information to its shareholders about an offer before the offer was ever made, created a harmful imbalance in the flow of information to target shareholders).

49 The Senate report on the bill that became the Exchange Act is quite explicit on this point:

It is contemplated that the rules and regulations promulgated by the Commission will protect investors from promiscuous solicitation of their proxies, on the one hand, by irresponsible outsiders seeking to wrest control of a corporation away from honest and conscientious corporation officials, and, on the other hand, by unscrupulous corporate officials seeking to retain control of the management by concealing and distorting facts.

S. REP. NO. 1455, 73d Cong., 2d Sess. 77 (1934).

50 The SEC submitted numerous comments on S. 2731 to Senator Williams along with a revised version of the bill. *See* 112 CONG. REC. 19,003-07 (1966).

51 The final version of S. 510 reflected the SEC's suggested changes and contained further modifications added during the hearings on the bill. *See* 113 CONG. REC. 854-57 (1966); Hamilton, *supra* note 38, at 275-76. The provisions of S. 510 that attempted to neutralize S. 2731 were as follows: first, the prior-notice mandate was dropped, and S. 510 adopted the concurrent disclosure requirement of § 14(d)(1). Second, S. 510 granted the SEC rulemaking power in § 14(d)(4) to regulate target management countersolicitations. Third, S. 510 added § 14(e), the antifraud provision, which was made applicable to the offeror and opponents of the tender offer. Finally, S. 510 gave the SEC authority in § 13(e) to impose a regulatory scheme on a corporation's purchas-

Senator Williams explained: "We have taken extreme care to avoid tipping the scales in favor of management or in favor of the person making the takeover bids."⁵²

As subsequently enacted in 1968, the Williams Act had two intertwined objectives: protecting investors through disclosure of information, and preserving the viability of the tender offer process through regulatory neutrality.⁵³ Congress sought to provide target shareholders with full and balanced disclosure of information and sufficient time to evaluate this information so that they would be able to make an unhurried, informed choice. Congress also sought to avoid tipping the balance of regulation in favor of the offeror or target management so that target shareholders would not be effectively deprived of an opportunity to make the choice. Guided by these twin objectives, the Act provided an evenhanded solution for the market problems stemming from tender offers and the tactics used to thwart them and established standards of conduct for all participants in the tender offer process.

es of its own shares. See 112 CONG. REC. 19,003-07 (1966); Note, *Cash Tender Offers*, 83 HARV. L. REV. 377, 381 n.28 (1969) [hereinafter Note, *Cash Tender Offers*]; Note, *Private Litigation Under the Williams Act: Standing to Sue, Elements of a Claim and Remedies*, 7 J. CORP. L. 545, 548 n.31 (1982) [hereinafter Note, *Standing to Sue*]; Note, *Cash Tender Offers: A Proposed Definition*, 31 U. FLA. L. REV. 694, 701 n.56 (1979) [hereinafter Note, *A Proposed Definition*].

⁵² 113 CONG. REC. 24,664 (1967).

⁵³ The House and Senate reports appear to indicate that the two purposes are of equal importance, although the point is arguable. The evolution of the Williams Act manifests a congressional attempt to create a comprehensive legislative scheme that would both protect investors and preserve the viability of tender offers as a method of corporate acquisition. While neutrality was perceived by Congress as a principal means of providing investor protection, it was also viewed as a distinct goal that Congress was apparently unwilling to subordinate, particularly after it had so painstakingly avoided "tipping the balance" in favor of either the target or offeror. See H.R. REP. NO. 1711, *supra* note 2, at 4, reprinted in 1968 U.S. CODE CONG. & ADMIN. NEWS at 2813; S. REP. NO. 550, *supra* note 5, at 3; see also Note, *Standing to Sue*, *supra* note 51, at 548-59; *infra* note 177. But see Note, *Tender Offer Regulation—Injunction Standards Under the Williams Act*, 45 FORDHAM L. REV. 51, 54 (1976) (arguing that investor protection is the predominant purpose); Note, *Cash Tender Offers*, *supra* note 51, at 700 (same). For a discussion of the Supreme Court's view on the purposes of the Williams Act, see *infra* text accompanying notes 162-66. Some legal commentators contend that the Williams Act is not neutral, but they disagree on which side the Act favors. Compare Booth, *The Problem With Federal Tender Offer Law*, 77 CALIF. L. REV. 707, 715 (1989) (the Williams Act favors the bidder) with Fischel, *From MITE to CTS: State Anti-Takeover Statutes, the Williams Act, the Commerce Clause, and Insider Trading*, 1987 SUP. CT. REV. 47, 72-73 (the Williams Act favors target management).

B. Overview of the Statute

The Williams Act added sections 13(d)-(e) and sections 14(d)-(f) to the Exchange Act,⁵⁴ and these sections were amended into their current form in 1970.⁵⁵ The major provisions relating to tender offers⁵⁶ are contained in sections 14(d), 14(e), and 13(e).

54 See *supra* note 8. In general, the Williams Act and the SEC rules thereunder are applicable only to acquisitions of a class of equity security registered pursuant to § 12 of the Exchange Act, 15 U.S.C. § 78l (1988). See *id.* §§ 78m(d)(1), 78m(e)(1), 78n(f). But see *infra* notes 58-59 & 106.

55 Act of Dec. 22, 1970, Pub. L. No. 91-567, 84 Stat. 1497 (codified at 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(e) (1988)). The 1970 amendments, among other things, extended the strictures of § 14(d) to exchange tender offers by deleting the 1968 exemption in § 14(d) for offers pursuant to a Securities Act registration statement. Consequently, exchange tender offers are governed by both the Securities Act and the Williams Act. *Id.* § 4, 84 Stat. at 1497 (codified at 15 U.S.C. § 78n(d)).

56 Congress intentionally left open the question of what types of purchases are encompassed by the operative term "tender offer." See *Takeover Bids: Hearings on H.R. 14475, S. 510 Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce, 90th Cong., 2d Sess. 13 (1968) [hereinafter House Hearings]* (statement of Manuel F. Cohen, Chairman, SEC). Both the statutory provisions themselves and the legislative history indicate, however, that Congress was primarily focusing on "conventional" tender offers when it passed the Williams Act. See Note, *The Developing Meaning of "Tender Offer" Under the Securities Exchange Act of 1934*, 86 HARV. L. REV. 1250, 1260-61 (1973). Yet, the legislative documents also suggest that Congress contemplated that the Act would extend beyond orthodox tender offers to encompass certain open market and privately negotiated purchases of securities when such an extension was necessary to effectuate the statute's purposes. See 113 CONG. REC. 854, 856 (1967) (remarks of Sen. Williams).

Although the SEC has authority to promulgate an interpretive rule defining the term "tender offer," it cannot seem to make up its mind whether a definition is appropriate or feasible. See Comment, *Toward a Definition of "Tender Offer"*, 19 HARV. J. ON LEGIS. 191, 207-08 n.62 (1982); Note, *A Proposed Definition, supra* note 51, at 704. In 1976, the SEC investigated the possibility of defining a "tender offer" but found there was no consensus on the meaning of the term. Notice of Proposed Tender Offer Rules and Schedules, Exchange Act Release No. 12,676, [1976-1977 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 80,659, at 86,695-96 (Aug. 2, 1976). Several years later, the SEC again considered and rejected defining the term. Proposed Tender Offer Rules and Schedule, Exchange Act Release No. 15,548, [1979 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 81,935, at 81,213 (Feb. 5, 1979). Then, in late 1979, the SEC released for public comment a proposed rule that defined the term. Proposed Amendments to Tender Offer Rules, Exchange Act Release No. 16,385, [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,374, at 82,601-06 (Nov. 29, 1979). The proposed rule, however, was never adopted. By and large, the SEC, like Congress, seems reluctant to define the term, largely out of a realization that once a definition is put in place, purchasers whose transactions may well warrant the regulation which §§ 14(d) and 14(e) provide may be able to structure the transactions so as to evade the application of these Williams Act provisions.

Because the SEC has never adopted a precise regulatory definition, the task has been delegated to the federal courts for determination on a case-by-case basis. Since 1979, most courts, however, have been guided by a test proposed by the SEC in *Wellman v. Dickinson*, 475 F. Supp. 783, 823-24 (S.D.N.Y. 1979), *aff'd*, 682 F.2d 355 (2d

These three sections will be discussed more fully below, but in brief, section 14(d) regulates third-party tender offers,⁵⁷ section 14(e) is the general antifraud/antimanipulation provision for all tender offers,⁵⁸ and section 13(e) governs a company's purchase of its own securities, including by way of tender offer.⁵⁹ Section 13(d) regulates sizeable acquisitions of a company's securities by a third party if the securities are not acquired by means of a tender offer,⁶⁰ and section 14(f) governs transactions subject to section

Cir. 1982), *cert. denied*, 460 U.S. 1069 (1983). The test lists eight factors that are characteristic of a tender offer, and courts utilizing this SEC profile have indicated that all eight factors need not be present to find a tender offer. *See, e.g., id.* at 824; Hoover Co. v. Fuqua Indus., [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,107, at 96,148 (N.D. Ohio June 11, 1979). The Second Circuit, however, in *Hanson Trust v. SCM Corp.*, 774 F.2d 47 (2d Cir. 1985), trumped the SEC's eight-factor test, stating that "the elevation of [the test] to a mandatory 'litmus test' seemed unwise and unnecessary." *Id.* at 56-57. Rather, the court concluded that a tender offer exists whenever the solicitees need the protections of § 14(d). *Id.* at 57-58.

The difficulty in drawing a bright line between those acquisitions that are tender offers and those that are truly open market and privately negotiated purchases is of little solace to corporate planners advising clients who intend to embark on substantial buying programs. For if advice that no tender offer will be involved turns out to be wrong, the acquiror may face an SEC enforcement suit sterilizing the shares purchased or rescinding the entire transaction for failure to comply with § 14(d) in executing the transaction. *See* 15 U.S.C. § 78u(d) (1988) (granting the SEC authority to institute enforcement suits); 1 T. HAZEN, THE LAW OF SECURITIES REGULATION § 11.18, at 736 (2d ed. 1989) (stating that a violation of § 14(d) may give rise to an implied right of action for private injunctive relief).

57 Section 14(d) applies only if after consummation of the tender offer, the offeror will own more than five percent of the class of securities sought. 15 U.S.C. § 78n(d)(1) (1988). Also, issuer tender offerors are specifically exempted from § 14(d). *Id.* § 78n(d)(8)(B).

58 It is the SEC's position that § 14(e) applies to every tender offer, even those not subject to § 14(d). *See supra* note 54. Thus, under the SEC's view, § 14(e), applies to tender offers for unregistered equity securities and debt securities whether or not registered under § 12 of the Exchange Act. *See* Adoption of Amendments to Tender Offer Rules, Exchange Act Release No. 16,384, [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,373, at 82,577 (Nov. 29, 1979); Proposed Amendments to Tender Offer Rules, Exchange Act Release No. 16,385, *supra* note 56, at 82,601. *But see* L.P. Acquisition Co. v. Tyson, 616 F. Supp. 1186, 1188-90 (E.D. Mich.) (holding that "the scope of § 14(e) is limited to tender offers for registered equity securities"), *rev'd in part, vacated in part, on other grounds*, 772 F.2d 201 (6th Cir. 1985); Conard, *Tender Offer Fraud: The Secret Meaning of Subsection 14(e)*, 40 BUS. LAW. 87, 89-95 (1984) (arguing that Congress was not conscious of a difference in coverage between § 14(e) and any other section of the Williams Act).

59 All issuers that have a class of equity securities registered pursuant to § 12 are subject to § 13(e), and § 13(e) applies to purchases by such issuer of any of its equity securities. 15 U.S.C. § 78m(e) (1988).

60 Section 13(d) requires any person, after acquiring more than five percent of a corporation's securities, to file with the SEC and to furnish the corporation, within 10 days of the acquisition, essentially the same information that a tender offeror must supply under § 14(d). *Id.* § 78m(d)(1); *see infra* text accompanying note 66. The information

13(d) or section 14(d) when the transactions contain a private agreement for the transfer of control.⁶¹ Pursuant to authority contained in the Williams Act,⁶² the SEC adopted rules in 1968 to implement this statutory structure.⁶³ These skeletal, emergency rules have evolved over the last two decades into a detailed regulatory scheme governing both tender offers and sizeable acquisitions of securities.⁶⁴

C. The Major Tender Offer Provisions

1. Section 14(d)

Section 14(d) establishes the primary disclosure obligations of the tender offeror. Upon making a tender offer to the target shareholders, the offeror must file with the SEC, and furnish the target company, detailed information about itself and the offer.⁶⁵ In general, the required disclosures include the identity and background of the offeror, the source and amount of funds or other consideration to be used in making the purchases, the extent of

must also be sent to each national securities exchange where the securities are traded. 17 C.F.R. § 240.13d-1 (1990). Section 13(d) does not apply to issuer repurchases. 15 U.S.C. § 78m(d)(6)(C) (1988). The purpose of § 13(d) is to alert the marketplace to new aggregations of stock holdings that might represent a potential change in corporate control. *GAF Corp. v. Milstein*, 453 F.2d 709, 717 (2d Cir. 1971), *cert. denied*, 406 U.S. 910 (1972); *see Comment, Section 13(d) and Disclosure of Corporate Equity Ownership*, 119 U. PA. L. REV. 853, 871 (1971). Although the open market and privately negotiated purchases governed by § 13(d) are frequently a harbinger of a § 14(d) tender offer, there are significant differences in the regulation of the two types of acquisitions. Under § 13(d), the required disclosure of information is made after the acquisition, whereas under § 14(d), it is made concurrently with the commencement of the offer. Further, § 13(d), unlike § 14(d), contains no provisions regulating the fairness of the transaction. *See infra* text accompanying notes 83-88. Finally, there is no specific antifraud provision, comparable to § 14(e), applicable to § 13(d)-regulated purchases. Rule 10b-5, 17 C.F.R. § 240.10b-5 (1990), however, may apply to purchases governed by § 13(d).

61 Under § 14(f), if there is a private agreement that a majority of the directors will be designated or elected (otherwise than at a shareholder meeting) after the acquisition, the corporation must file with the SEC and send to its shareholders a statement containing the same type of information that would be required under the proxy rules if the persons so designated or elected were nominees for election as directors at a meeting of shareholders. 15 U.S.C. § 78n(f) (1988); *see* 17 C.F.R. § 240.14f-1 (1990). *See also* Ratner, *Section 14(f): A New Approach to Transfers of Corporate Control*, 54 CORNELL L. REV. 65 (1968).

62 *See supra* note 14.

63 *See* 17 C.F.R. §§ 240.13d-1, .13d-2, .13d-101 (sched. 13D), .13e-1, .14d-1 to .14d-4, .14d-101, .14f-1 (1968).

64 *See id.* §§ 240.13d-1 to .13d-7, .13d-101 (sched. 13D), .13e-1, .13e-3, .13e-4, .13e-100 (sched. 13E-3), .13e-101 (sched. 13E-4), .14d-1 to .14d-10, .14d-100 (sched. 14D-1), .14d-101 (sched. 14D-9), .14e-1 to .14e-3, .14f-1 (1990).

65 15 U.S.C. § 78n(d)(1) (1988).

the holdings of the offeror in the target company, and the purpose of the purchases.⁶⁶ The offer itself and any subsequent solicitations made to the target shareholders by the offeror must also be filed with the SEC and delivered to the target company.⁶⁷ In a series of rules adopted under section 14(d), the SEC has augmented considerably this statutory framework.⁶⁸ Rule 14d-3⁶⁹ provides more specific filing and transmission requirements;⁷⁰ rule 14d-6⁷¹ sets forth information that must be disclosed in the offer and subsequent solicitations made to the target shareholders;⁷² and rules 14d-4⁷³ and 14d-5⁷⁴ establish three nonexclusive methods of disseminating the offer to the target shareholders:⁷⁵ long-form publication in a newspaper, summary

66 Section 14(d) requires disclosures of the type specified in § 13(d), in addition to other information the SEC may require. *Id.*

67 *Id.*

68 Rule 14d-1, defines terms frequently used in the rules adopted under § 14(d) (regulation 14D) and under § 14(e) (regulation 14E). 17 C.F.R. § 240.14d-1 (1990). Rule 14d-2, which triggers the operation of regulation 14D, defines the "date of commencement of a tender offer" as essentially the date the tender offer is first published or sent or given to target shareholders. *Id.* § 240.14d-2. Under rule 14d-2(b), however, an offeror may make a public announcement of the offer as long as it complies with the filing, dissemination, and disclosure obligations of regulation 14D within five business days. *Id.* § 240.14d-2(b). Safe harbor provisions for brief public announcements that do not constitute rule 14d-2(b) public announcements are set forth in rule 14d-2(d)-(e). *Id.* § 240.14d-2(d)-(e). One of the major purposes of rule 14d-2 was to create a conflict between the rule and those state takeover statutes, pre-MITE, that imposed a precommencement waiting period. The conflict buttressed the SEC's preemption argument. *See infra* notes 399-402 and accompanying text. The events in the MITE litigation, however, preceded the adoption of rule 14d-2. *Edgar v. MITE Corp.*, 457 U.S. 624, 636 n.11 (1982).

69 17 C.F.R. § 240.14d-3 (1990).

70 The information filed with the SEC and transmitted to the target company by the offeror is called a tender offer statement. The information that must be disclosed in this statement is set forth in schedule 14D-1, *id.* § 240.14d-100. *See id.* § 240.14d-3(a). The tender offer statement must also be sent to any competing bidder, to each national securities exchange where the securities sought are listed, and the National Association of Securities Dealers, Inc. (NASD) if the securities sought are quoted in NASDAQ. *See id.* § 240.14d-3(a).

71 *Id.* § 240.14d-6.

72 The information that must be disclosed to the target shareholders depends on the method used by the offeror to disseminate the offer. In general, the required disclosures include major portions of the tender offer statement. *See id.* § 240.14d-6(c).

73 *Id.* § 240.14d-4.

74 *Id.* § 240.14d-5.

75 Information disseminated in compliance with rule 14d-4 is deemed "published, sent or given to security holders" for purposes of § 14(d)(1). The dissemination of an exchange tender offer is governed by the Securities Act if the transaction has to be registered. Adoption of Amendments to Tender Offer Rules, Exchange Act Release No. 16,384, *supra* note 58, at 82,585. Further, when the exchange tender offer is registered, the prospectus must contain information about both the offeror and the target, which

advertisement in a newspaper,⁷⁶ and use of a shareholder list. If the offeror chooses the shareholder list method of dissemination—a method that had been developed by the SEC for proxy contests in rule 14a-7⁷⁷—the target company is given the option either to furnish the list to the offeror or to mail the offeror's materials to the target shareholders at the offeror's expense.⁷⁸ The elaborate scheme of disclosure obligations imposed on the tender offeror under section 14(d) is designed to ensure that information about the offeror and its qualifications is made publicly available and that the target shareholders are able to respond to the offer with actual knowledge of this information.

To maintain a neutral regulatory balance, section 14(d) also governs solicitations and recommendations in connection with the tender offer that are made to target shareholders by the target company and other tender offer participants. The SEC is given specific rulemaking power to regulate these communications;⁷⁹ and at present, rule 14d-9—patterned after rule 14a-11, a special proxy rule applicable to contested elections⁸⁰—establishes filing,

presents some difficulties for the offeror when target management is not cooperative. See L. LOSS, *supra* note 3, at 498.

76 If an offeror uses a summary advertisement to disseminate the offer, the offeror must furnish its tender offer materials to any target shareholder on request. 17 C.F.R. § 240.14d-4(a)(2) (1990).

77 *Id.* § 240.14a-7. Under rule 14a-7, if a nonmanagement group wishing to solicit proxies requests a shareholder list, management must furnish the list or mail the nonmanagement group's proxy materials. The rule only applies, however, if management has solicited proxies or intends to solicit proxies. Moreover, the nonmanagement group must bear the cost of any expenses incurred.

78 *See id.* § 240.14d-5. Rule 14d-5 is based on the SEC's rulemaking power under § 14(d) and § 14(e). *See* Proposed Tender Offer Rules and Schedule, Exchange Act Release No. 15,548, *supra* note 56, at 81,225-27; *supra* note 14 and accompanying text; *infra* text accompanying note 95. Rule 14d-4 provides that any offeror that makes an adequate publication in a newspaper of a long-form publication or of a summary advertisement may use the shareholder list method of dissemination described in rule 14d-5. 17 C.F.R. § 240.14d-4(a)(3) (1990). During the first year of its effectiveness (1980), rule 14d-5 was rarely used. Since most tenders are made by arbitrageurs who purchase their shares during the course of the tender offer, the offerors presumably did not consider the added cost of dissemination using a shareholder list worthwhile. *See* R. JENNINGS & H. MARSH, *SECURITIES REGULATION* 690 n.1 (6th ed. 1987).

79 15 U.S.C. § 78n(d)(4) (1988).

80 17 C.F.R. § 240.14a-11 (1990). Rule 14a-11, which applies only to solicitations involving contests for the election or removal of directors, requires every "participant" (except the company) in such solicitations to file with the SEC and each national securities exchange where securities of the company are listed information regarding the identity and background of the participant and the participant's interests in securities of the company. *See id.* § 240.14a-11(c), -102 (sched. 14B). Each shareholder solicited must receive a summary of the greater part of this information. *See id.* § 240.14a-11(d)(3). Fur-

transmission, and disclosure requirements for the target and certain specified persons related to the target or the offeror.⁸¹ Upon making a solicitation or recommendation to target shareholders, the regulated party must provide the shareholders with detailed information about itself and the nature of the solicitation or recommendation. Also, this information and certain other disclosures must be filed with the SEC and furnished to the offeror and the target (if the target is not the party making the communication).⁸² Rule 14d-9 is aimed at assisting target shareholders in evaluating the merits of the solicitation or recommendation and in assessing the interest of the party making the communication.

Section 14(d) and the rules thereunder are not limited to disclosure. They also regulate the terms under which the offer must be conducted by conferring valuable rights on target shareholders. The explicit statutory rights which have been amplified by SEC rules are as follows: first, target shareholders who tender their shares may withdraw them while the offer is still open and, if the offeror has not purchased their shares, any time after sixty calendar days from the commencement of the offer. (Section 14(d) provides that shareholders may withdraw their tendered

ther, rule 14a-11 carves out an exception from the general requirement of the proxy rules by allowing either side to solicit proxies before furnishing a proxy statement in certain situations. *See id.* § 240.14a-3(a), -11(d).

81 *Id.* § 240.14d-9.

82 The information filed with the SEC and furnished to the offeror and the target is called a tender offer solicitation/recommendation statement. The information that must be disclosed in this statement is set forth in schedule 14D-9, *id.* § 240.14d-101. *See id.* § 240.14d-9(a). The solicitation/recommendation statement must also be sent to each national securities exchange where the securities being sought in the tender offer are listed and to NASD if the securities sought are quoted in NASDAQ. *See id.* §. The target shareholders must receive at least a summary of major portions of the information disclosed in this statement. *See id.* § 240.14d-9(c).

There is, however, an exemption from all the requirements of rule 14d-9 for the target company's initial, limited communication regarding the tender offer—the stop-look-and-listen communication. *See id.* § 240.14d-9(e). A target company relying on this exemption must state in the communication that on or before a specified date (which cannot be later than 10 business days from the commencement of the offer) it will advise the target shareholders of its position with respect to the offer. This subsequent communication, which is required in any event, will be a solicitation or recommendation subject to rule

14d-9. *See id.* § 240.14d-9(f); *infra* text accompanying note 99. Juxtaposed, the stop-look-and-listen communication exemption for targets in rule 14d-9(e) and the public announcement exemption for offerors in rule 14d-2(b) (*see supra* note 68) maintain a neutral regulatory balance: they both allow the regulated party to initiate its defense or offense largely unregulated. Furthermore, by way of rough analogy, the exception in proxy rule 14a-11, 17 C.F.R. § 240.14a-11 (1990) (allowing solicitations prior to furnishing a written proxy statement), comes to mind. *See supra* note 80.

shares at any time until the expiration of seven calendar days after the commencement of the offer, but rule 14d-7 extends the withdrawal period to the life of the offer.)⁸³ Second, if the tender offer is for less than all the outstanding shares (a partial offer) and more than the requested number of shares is tendered, the offeror must purchase the shares pro rata. (Section 14(d) limits the proration requirement to shares tendered during the first ten calendar days of the offer, but rule 14d-8 extends the proration requirement to the life of the offer.)⁸⁴ Third, if the offering price is increased, the offeror must pay the increased price to all tendering shareholders.⁸⁵ The SEC has taken the initiative to flesh out section 14(d) with two additional substantive requirements that are intended to prevent offerors from discriminating among target shareholders. Both of these requirements are contained in rule 14d-10.⁸⁶ First, a tender offer must be open to all target shareholders owning the class of securities sought in the offer.⁸⁷ Second, all target shareholders must be paid the highest

83 15 U.S.C. § 78n(d)(5) (1988); 17 C.F.R. § 240.14d-7 (1990). Pursuant to statutory authority contained in § 14(d)(5), the SEC in 1979 extended the withdrawal period to the first 15 business days of the offer and established a withdrawal right of 10 business days after the commencement of a competing offer. Adoption of Amendments to Tender Offer Rules, Exchange Act Release No. 16,384, *supra* note 58, at 82,591. In 1986, the SEC extended the withdrawal period to the life of the offer, and withdrawal rights upon commencement of a competing bid were eliminated. Adoption of All-Holders and Best-Price Rule, Exchange Act Release No. 23,421, [1986-1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,016, at 88,197 (July 11, 1986).

84 15 U.S.C. § 78n(d)(6) (1988); 17 C.F.R. § 240.14d-8 (1990). Section 14(d)(6) was specifically designed to reduce the pressure on target shareholders to deposit their shares hastily when the offer was made on a first-come, first-served basis. 113 CONG. REC. 856 (1967). The extension of the proration period to the life of the offer by the SEC in 1982 was deemed necessary because public shareholders had problems receiving the offering materials and making an investment decision during the statutory 10-calendar-day proration period. See Adoption of Pro Rata Rule, Exchange Act Release No. 19,336, [1982-1983 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,306, at 85,651 (Dec. 15, 1982). Because § 14(d)(6), unlike § 14(d)(5), does not grant the SEC rulemaking authority, rule 14d-8 was based, for the most part, on the SEC's rulemaking power under § 14(e). See *id.* at 85,652; *infra* note 378.

85 15 U.S.C. § 78n(d)(7) (1988). The statutory increased-price provision becomes particularly significant if several transactions are integrated as parts of a single tender offer. I T. HAZEN, *supra* note 56, § 11.14, at 713-14; see L. LOSS, *supra* note 3, at 513.

86 17 C.F.R. § 240.14d-10 (1990). Rule 14d-10, which contains the best-price and the all-holders requirements, was not adopted by the SEC until 1986. The rule was adopted primarily under §§ 14(d) and 14(e). See Adoption of All-Holders and Best-Price Rule, Exchange Act Release No. 23,421, *supra* note 83, at 88,188. The SEC contends, however, that the protections provided by rule 14d-10 are implicit in § 14(d). See Proposed Amendments Regarding Equal Treatment of Target Shareholders, Exchange Act Release No. 22,198, [1984-1985 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,797, at 87,560-61 (July 1, 1985); *infra* text following note 381.

87 17 C.F.R. § 240.14d-10(a)(1) (1990). The all-holders requirement of rule 14d-10

consideration paid to any other shareholder during the offer.⁸⁸ The substantive regulatory scheme of section 14(d)—which amounts to federal corporation law—is designed to ensure that target shareholders are treated fairly and that they have adequate time to consider the communications from both the offeror and target management in deciding whether to tender, sell into the market, or retain all or part of their securities.

2. Section 14(e)

Section 14(e) has two prongs. The first prong, which is borrowed from rule 14a-9, the proxy antifraud rule,⁸⁹ makes it unlawful for anyone to make untrue or misleading statements in connection with any tender offer.⁹⁰ The second prong, which resembles section 10(b) of the Exchange Act,⁹¹ makes it unlawful for anyone to engage in fraudulent, deceptive, or manipulative acts or practices in connection with any tender offer.⁹² An all-encompassing provision, section 14(e) is directed at the conduct of the offeror, the target company, and any other tender offer participant that is seeking to influence the target shareholders'

does not prevent an offeror from making a tender offer that excludes all shareholders in a state where the offeror is prohibited from making the tender offer by governmental action pursuant to a state statute, as long as the offeror has in good faith tried to comply with the statute. *Id.* § 240.14d-10(b)(2).

88 *Id.* § 240.14d-10(a)(2). The best-price provision of rule 14d-10 does not, however, prohibit more than one type of consideration as long as shareholders are permitted to elect among each type and the highest consideration of each type paid to any shareholder is paid to any other shareholder receiving that type of consideration. *Id.* § 240.14d-10(c). The best-price provision is designed, for example, to prevent a bidder from paying a higher consideration to the employee-shareholders of the target company than it is paying to other shareholders. See Proposed Amendments Regarding Equal Treatment of Target Shareholders, Exchange Act Release No. 22,198, *supra* note 86, at 87,563 n.13. Also, if the bidder decreases the offering price (for example, because the target company sells a significant portion of its assets to a third party as a defensive measure), the best-price provision requires that the bidder pay the decreased price to all target shareholders—those who tendered before the decrease in price (but did not withdraw their shares) and those who tendered after the decrease in price. See Proposed All-Holders and Best-Price Rule, Exchange Act Release No. 22,791, [1985-1986 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,955, at 87,981 (Jan. 14, 1986). In the release adopting rule 14d-10, the SEC indicated that the best-price provision would allow a bidder to reduce the offering price without having to terminate the offer and commence a new offer, as had previously been required. Adoption of All-Holders and Best-Price Rule, Exchange Act Release No. 23,421, *supra* note 83, at 88,187.

89 17 C.F.R. § 240.14a-9 (1990).

90 15 U.S.C. § 78n(e) (1988). The first prong of § 14(e) does not track rule 14a-9 exactly. For example, rule 14a-9 refers to "false" rather than "untrue" statements.

91 *Id.* § 78j(b).

92 *Id.* § 78n(e).

choice or the outcome of the offer.⁹³ Hence, it covers, for example, the disclosures required by section 14(d) and the offensive or defensive tactics that may be used in the contest.⁹⁴

The efficacy of section 14(e) was substantially enhanced by the 1970 amendments to the Williams Act, which gave the SEC rulemaking power to define and prescribe means reasonably designed to prevent the fraudulent, deceptive, or manipulative practices prohibited by section 14(e).⁹⁵ And pursuant to this authority, the SEC has adopted two prophylactic rules that are central to the regulatory scheme for tender offers. These rules add to the disclosure requirements and substantive protections of section 14(d) and create more federal corporation law. In these rules, the SEC has singled out for regulation two abusive tender offer practices that had developed in takeover battles: an unnegotiated, surprise tender offer of short duration (the so-called "blitzkrieg" or "Saturday night special") and target management's silence on its position regarding an offer when silence maximized a tactical advantage. First, under rule 14e-1, all tender offers must be held open at least twenty business days.⁹⁶ Also, upon the announcement of an increase or decrease in the percentage of securities sought or the consideration offered, the offer must remain open for ten business days.⁹⁷ Second, under rule 14e-2, within ten business days of the commencement of a tender offer, a target company must publish or send to its shareholders a reasoned statement indicating that it recommends acceptance or rejection of the offer, is remaining neutral, or is unable to take a position.⁹⁸ Because the target's statement of position pursuant to this rule constitutes a solicitation or recommendation within the mean-

93 Furthermore, § 14(e) may apply before a tender offer formally commences, as in the case of a "creeping" tender offer. *SEC v. Gaspar*, [1984-1985 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 92,004, at 90,979 (S.D.N.Y. Apr. 15, 1985) (citing cases).

94 Litigation under § 14(e) is a tactic itself, even if standing to sue is denied. See L. Loss, *supra* note 3, at 527-28 ("Section 14(e) is beginning to rival Rule 10b-5 as the subject of litigation. It would not be an exaggeration to say that there has hardly been a contested tender offer in which both sides have not hurled § 14(e) thunderbolts at each other." (footnote omitted)).

95 Act of Dec. 22, 1970, Pub. L. No. 91-567, sec. 5, §-14(e), 84 Stat. 1497, 1497-98 (codified at 15 U.S.C. § 78n(e) (1988)).

96 17 C.F.R. § 240.14e-1(a) (1990).

97 *Id.* § 240.14e-1(b). In addition, the offeror must pay the consideration offered or return the securities deposited promptly after the offer is terminated or withdrawn. *Id.* § 240.14e-1(c).

98 *Id.* § 240.14e-2.

ing of section 14(d),⁹⁹ the target must also comply with rule 14d-9.¹⁰⁰

3. Section 13(e)

By and large, the Williams Act left unregulated a company's purchases of its own securities. Section 13(e), however, gives the SEC broad rulemaking power to regulate these repurchases. Specifically, the SEC is authorized to define fraudulent, deceptive, or manipulative acts and practices that might occur in connection with an issuer repurchase program, and to adopt means reasonably designed to prevent such acts and practices.¹⁰¹

The SEC has not used its section 13(e) rulemaking authority to regulate all issuer repurchases.¹⁰² Yet, it has adopted two rules under section 13(e) that are critical to the tender offer regulatory scheme. Rule 13e-1 prohibits a target company from purchasing its securities during a third party's tender offer for its shares unless a statement is filed with the SEC by the target and the target shareholders have received (within the past six months) the substance of the information filed with the SEC.¹⁰³ The information that must be disclosed relates to the manner and purpose of the purchases and the source of funds to be used.¹⁰⁴ Thus, rule 13e-1 seeks to maintain a neutral balance by regulating the not uncommon tactic used by a target company to defeat an offer: repurchasing large quantities of its own securities in compe-

99 *Id.* § 240.14d-9(f).

100 In addition to rule 14e-1 and rule 14e-2, the SEC has adopted rule 14e-3, *id.* § 240.14e-3, under § 14(e). Rule 14e-3 outlaws certain "insider" trading transactions in connection with a tender offer by defining the transactions as "fraudulent," "deceptive," or "manipulative" practices within the meaning of § 14(e). Specifically, it prohibits tippees from the tender offeror or target from trading in target securities prior to public disclosure of the tender offer. *Id.* § 240.14e-3(a). Tipping per se is also prohibited as "a means reasonably designed to prevent" fraudulent, deceptive, or manipulative practices within the meaning of § 14(e). *Id.* § 240.14e-3(d).

101 15 U.S.C. § 78m(e)(1) (1988). Section 13(e) indicates that the § 13(e) rules may require the issuer to provide its shareholders with whatever information the SEC considers necessary or appropriate in the public interest or for the protection of investors, such as the reasons for the purchase, the source of funds, the number of shares to be purchased, the price, and the method of purchase. *Id.*

102 The SEC, however, has adopted rule 10b-18, 17 C.F.R. 240.10b-18 (1990), which provides a safe harbor for issuer repurchases. *See infra* note 282.

103 17 C.F.R. § 240.13e-1 (1990). In order for rule 13e-1 to apply, the third-party tender offer must be for a class of equity securities of an issuer that is subject to § 13(e) (*see supra* note 59), and the issuer must comply with the rule upon making purchases of any of its equity securities.

104 17 C.F.R. § 240.13e-1(a) (1990).

tion with the third-party offer, either through market transactions or by a tender offer for its own shares.¹⁰⁵ Furthermore, when the repurchases are sought by tender offer, rule 13e-4 imposes an additional layer of regulation.¹⁰⁶ Under rule 13e-4—which applies whether or not a third-party offer is outstanding—a company making a “self-tender” must comply with the same disclosure requirements, and grant its shareholders the same substantive rights, established in section 14(d), section 14(e),¹⁰⁷ and the rules thereunder for third-party tender offers.¹⁰⁸ In formulating rule 13e-4, the SEC took the position that section 13(e) did not limit it to adopting exclusively disclosure requirements and that some substantive regulation was necessary to prevent

105 Facially, this tactic may appear to be self-defeating, since the securities reacquired by the target cannot be voted and the amount of securities needed by the offeror to gain control will thereby be reduced. The collateral effects of the repurchases, however, should deter or thwart the offer. The target's repurchases may drive up the market price of the securities such that shareholders will sell in the market rather than tender, or the repurchases may substantially deplete the target's cash (or increase its debt) such that it is no longer an attractive target.

106 17 C.F.R. § 240.13e-4 (1990). Another layer of regulation is imposed by rule 13e-3, *id.* § 240.13e-3, if a “going private” transaction is involved, that is, if the effect of the repurchases or tender offer is cessation of reporting obligations under the Exchange Act. There is no rule 13e-2. Although § 13(e) applies only to issuers that have a class of equity securities registered under § 12 of the Exchange Act (*see supra* note 59), the SEC has used its rulemaking authority under § 10(b) of the Exchange Act to extend the coverage of rule 13e-3 and rule 13e-4 to issuers that merely have reporting obligations under § 15(d) of the Exchange Act, 15 U.S.C. § 78o(d) (1988). *See* 17 C.F.R. § 240.13e-3(c), -4(a) (1990).

107 Even in the absence of rule 13e-4, § 14(e) would apply to issuer tender offers. *See* *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579, 595-96 (5th Cir.), *cert. denied*, 419 U.S. 873 (1974); Adoption of Amendments to Tender Offer Rules, Exchange Act Release No. 16,384, *supra* note 58, at 82,581; *see also* Henry Heide, Inc., [1972-1973 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,838, at 81,836 (May 1, 1972).

108 In brief, rule 13e-4 first defines “fraudulent, deceptive, and manipulative acts and practices” simply as fraud, deception, and manipulation, borrowing the exact language of rule 10b-5, 17 C.F.R. § 240.10b-5 (1990). *Id.* § 240.13e-4(b)(1). In effect, rule 13e-4 then goes on to provide that as means reasonably designed to prevent such acts or practices in connection with an issuer tender offer, the issuer must comply with the provisions applicable to third-party tender offers. *Id.* § 240.13e-4(b)(2)-(f)(11). There is one rule 13e-4 requirement, not applicable to third-party tender offers, that stands out: after terminating a self-tender, an issuer is subject to a cooling-off period of 10 business days before it is allowed to purchase in the market any of its securities which were sought in the offer. *Id.* § 240.13e-4(f)(6). According to the SEC, rule 13e-4(f)(6) is an “antimanipulation” provision designed to prevent the issuer from supporting an artificial market price for its securities (that were the subject of the offer) after termination. *See* Adoption of Rules Regarding Tender Offers by Issuers, Exchange Act Release No. 16,112, [1979 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,182, at 82,210 (Aug. 16, 1979).

fraudulent, deceptive, or manipulative conduct which may occur in the absence of such regulation.¹⁰⁹

II. STANDING TO SUE UNDER THE WILLIAMS ACT

A. *Enforcement of the Williams Act: A Preliminary View*

Although Congress and the SEC carefully crafted the Williams Act regulatory scheme, neither the statute nor the rules contain an explicit reference to enforcement. The incorporation of the Williams Act provisions into the Exchange Act, however, makes sections 21(d)¹¹⁰ and 32(a)¹¹¹ of the Exchange Act applicable to Williams Act transgressions. Under section 21(d), the SEC may institute enforcement proceedings to enjoin violations, and section 32(a) imposes criminal penalties when the violations are willful. Also applicable to the Williams Act is section 18¹¹² of the Exchange Act, one of the Act's three express civil liability provisions. Section 18 establishes a modicum of private enforcement by imposing liability on anyone who makes an Exchange Act filing that contains a false or misleading statement. The liability runs only in favor of a person who purchases or sells securities "at a price which was affected by such statement," and the damages recoverable are those caused by reliance on the statement.¹¹³ Section 18 suits, therefore, could crop up whenever filings are required under any of the Williams Act provisions, but because of its strict reliance and causation requirements, section 18 has turned out to be almost a dead letter.¹¹⁴

At the time the Williams Act was adopted, it did not appear, however, that sections 21(d), 32(a), and 18 would be the exclusive means of enforcing the Act. The likelihood that the federal courts would permit implied private rights of action to supplement enforcement of the Act seemed high. The federal courts had been implying private rights of action, following a common-law tradition, long before the enactment of the first federal securities stat-

109 See Adoption of Rules Regarding Tender Offers by Issuers, Exchange Act Release No. 16,112, *supra* note 108, at 82,206.

110 15 U.S.C. § 78u(d) (1988).

111 *Id.* § 78ff(a).

112 *Id.* § 78r.

113 *Id.* § 78r(a). The plaintiff cannot know that the statement was false or misleading, and the defendant is relieved of liability if he proves "that he acted in good faith and had no knowledge that [the] statement was false or misleading." *Id.*

114 See Note, *Section 18 of the Securities Exchange Act of 1934: Putting the Bite Back into the Toothless Tiger*, 47 FORDHAM L. REV. 115, 116 (1978).

utes in 1933 and 1934;¹¹⁵ and by the time the Williams Act was on the books, the courts generally tended to favor the implication of private actions under the federal securities laws.¹¹⁶

B. The Implication of Private Rights of Action Under the Federal Securities Laws Before Piper

The first major decision dealing with implied rights of actions based on the federal securities laws, *Kardon v. National Gypsum Co.*,¹¹⁷ was rendered in 1946 by the District Court for the Eastern District of Pennsylvania.¹¹⁸ In *Kardon*, the court implied a private right of action for damages on behalf of a defrauded seller of securities under section 10(b)¹¹⁹ of the Exchange Act and rule 10b-5,¹²⁰ which ban the use of manipulative or deceptive devices in connection with the purchase or sale of any security but do not contain an express right to sue. The result in *Kardon* was predicated on the so-called tort theory for implying private rights of action. According to this theory, any person who breaches a statutory duty is liable to any injured member of the class for whose benefit the statute was intended.¹²¹ The *Kardon*

115 The idea of implying private actions from statutory provisions was invented by the English courts, and the doctrine was first used by the U.S. Supreme Court in *Texas & Pac. Ry. Co. v. Rigsby*, 241 U.S. 33 (1916). See L. LOSS, *supra* note 3, at 924-25; Schneider, *Implying Private Rights and Remedies Under the Federal Securities Acts*, 62 N.C.L. REV. 853, 853 (1984).

116 In general, the courts have ruled that a § 18 remedy is not exclusive. See 2 T. HAZEN, *supra* note 56, § 12.8, at 49 & n.21 (citing cases). In *Herman & MacLean v. Huddleston*, 459 U.S. 375 (1983), the Supreme Court held that implied civil liability under rule 10b-5, 17 C.F.R. § 240.10b-5 (1990), is not precluded by the express remedy of § 11 of the Securities Act, 15 U.S.C. § 77k (1988). Since § 18 is § 11's sister provision in the Exchange Act, it seems probable that the Supreme Court would rule that the remedies under rule 10b-5 and § 18 are also cumulative. *But see* Note, *The Exclusivity of the Express Remedy Under Section 18(a) of the Securities Exchange Act of 1934*, 46 GEO. WASH. L. REV. 845 (1978).

117 69 F. Supp. 512 (E.D. Pa. 1946).

118 The first decision holding that an implied right of action existed under the federal securities laws was *Baird v. Franklin*, 141 F.2d 238 (2d. Cir.), *cert. denied*, 323 U.S. 737 (1944). Prior to *Baird*, however, the courts had implied a damages remedy from a federal securities statute when the statute expressly authorized an equitable remedy. See, e.g., *Deckert v. Independence Shares Corp.*, 311 U.S. 282 (1940); *Geismar v. Bond & Goodwin, Inc.*, 40 F. Supp. 876 (S.D.N.Y. 1941).

119 15 U.S.C. § 78j(b) (1988).

120 17 C.F.R. § 240.10b-5 (1990).

121 See Pitt, *Standing to Sue Under the Williams Act After Chris-Craft: A Leaky Ship on Troubled Waters*, 34 BUS. LAW. 117, 162 n.333 (1978); see also R. JENNINGS & H. MARSH, *supra* note 78, at 836-37. In American jurisprudence, the tort theory emanates from *Texas & Pac. Ry. Co. v. Rigsby*, 241 U.S. 33 (1916). See *supra* note 115.

court stressed that a remedy should be implied under the theory unless there was a clear legislative intention that it should be denied.¹²² In 1971, in *Superintendent of Insurance v. Bankers Life & Casualty Co.*,¹²³ the Supreme Court unanimously recognized the holding in *Kardon* by explicitly acquiescing in what had become an overwhelming acceptance by the lower federal courts of implied actions under section 10(b) and rule 10b-5.¹²⁴ Moreover, the Court in *Bankers Life* took pains to note that there was redress under section 10(b), "whatever might be available as a remedy under state law."¹²⁵

Bankers Life was consistent with the Supreme Court's seminal decision in 1964, *J.I. Case Co. v. Borak*,¹²⁶ unanimously holding that an implied right of action existed under section 14(a)¹²⁷ of the Exchange Act and rule 14a-9,¹²⁸ the proxy antifraud provision. In *Borak*, a shareholder of the acquiring company in a merger sued those proposing the merger on the grounds that they had obtained the required shareholder approval by circulating false and misleading proxy solicitation material in violation of rule 14a-9. The shareholder-plaintiff, on behalf of himself and other shareholders similarly situated, sought rescission of the merger or damages. In ruling on the shareholder's claim, the Court examined the legislative history of section 14(a) under which rule 14a-9 was adopted and found that one of its "chief purposes" was to protect investors by preventing "management or others from obtaining authorization for corporate action by means of deceptive or inadequate disclosure in proxy solicitation."¹²⁹ The Court, however, was unable to point to any statements in the legislative record mentioning private rights of action. Nonetheless, the Court held that private rights of action for damages or injunctive relief were implicit in the statute because they were essential to accomplishing a legislative purpose *and* because they provided a necessary supplement to the SEC's efforts in enforcing the proxy rules.¹³⁰

122 *Kardon*, 69 F. Supp. at 512, 514 (E.D. Pa. 1946).

123 404 U.S. 6 (1971). Justice Douglas delivered the opinion for a unanimous Court.

124 *Id.* at 13 n.9 ("It is now established that a private right of action is implied under § 10(b).").

125 *Id.* at 12.

126 377 U.S. 426 (1964). Justice Clark wrote the opinion of the Court.

127 15 U.S.C. § 78n(a) (1988).

128 17 C.F.R. § 240.14a-9 (1990).

129 *Borak*, 377 U.S. at 431-32.

130 *Id.* at 431-33. The Court noted that the SEC examines over 2,000 proxy statements each year and that time does not permit an independent examination of each

Thus, as the basis for its decision, the Court relied on a variation of the tort theory utilized in *Kardon* and on the so-called effective enforcement theory of implying private rights of action: private actions should be implied when necessary to assist in the enforcement of the statute involved.¹³¹ Then, after noting that proxy violations also cause injury to the corporation, the Court held that the shareholder-plaintiff had standing to bring both direct and derivative actions under section 14(a).¹³²

In remanding the case for a trial on the merits, the *Borak* Court underlined the primary role of federal law in the remedial aspects of proxy regulation.¹³³ The Court emphasized that the district court had the power to grant all necessary remedial relief since federal law governed not only the propriety of the proxy solicitation material but also the validity of the solicited proxies and the consequences of invalidity, even though questions of state corporation law might ultimately be involved. In the same vein, the Court warned the district court that if the shareholder-plaintiff were merely granted a declaratory judgment (stating that false and misleading proxy solicitation material had been circulated in violation of rule 14a-9), he would be forced to turn to state law for retrospective relief; and if the state law happened to attach no responsibility to the use of false and misleading proxy solicitation material, the purpose of rule 14a-9 would be eviscerated.

Taking their cue from the *Borak* Court's expansive approach to the interpretation of the proxy rules, the lower courts have enlarged the class of plaintiffs that have standing to sue and have extended this grant of standing beyond the antifraud rule to the other proxy rules as well.¹³⁴ The courts have concluded that a

one. *Id.*

131 See Pitt, *supra* note 121, at 162 n.333. Actually, the Court framed the issue as whether § 27 of the Exchange Act, 15 U.S.C. § 78aa (1988), authorizes an implied private action for rescission or damages in favor of a shareholder to redress violations of § 14(a). But § 27 simply confers exclusive jurisdiction on the federal courts to hear actions brought under the Exchange Act.

132 *Borak*, 377 U.S. at 432.

133 *Id.* at 434-35. The Court, therefore, confused the subject matter jurisdiction question with the implication question. See Schneider, *supra* note 115, at 863-64; see also L. LOSS, *supra* note 3, at 929 ("[T]he Court reached the right result not for the wrong reason but for no reason at all."). The Court corrected its erroneous reading of § 27 in *Borak* 15 years later in *Touche Ross & Co. v. Redington*, 442 U.S. 560, 577 (1979) ("Section 27 creates no cause of action of its own force and effect; it imposes no liabilities.")

134 See, e.g., *Haas v. Wieboldt Stores*, 725 F.2d 71 (7th Cir. 1984) (rule 14a-7, 17 C.F.R. § 240.14a-7 (1990) (shareholder list rule)); *New York City Employees' Retirement Sys. v. American Brands*, 634 F. Supp. 1382 (S.D.N.Y. 1986) (rule 14a-8, 17 C.F.R.

corporation has standing to sue opposition groups, such as outsiders seeking control and insurgent shareholders involved in election contests or other contested matters.¹³⁵ Also, the courts have maintained that a group opposing management has standing to sue the corporation and that two groups, external to the corporation, have standing to sue each other.¹³⁶ Moreover, plaintiffs have been accorded standing to sue for both damages and a wide range of equitable remedies.¹³⁷ The judicial broadening of standing to sue under the proxy rules was based chiefly on *Borak's* policy of vigorous enforcement of the federal securities laws through private litigation. And regarding the two-way standing that has resulted, Professor Loss, the doyen among securities regulation scholars, has stated: "Either side in a contested [proxy] solicitation has a legitimate interest, in view of the statutory purpose, to cry 'Foul' against the other."¹³⁸

When litigation under the Williams Act came along, the lower courts assumed, with ample judicial precedent under sections 10(b) and 14(a) to draw upon, that implied rights of action existed under the various provisions of the new statute. Moreover, relying explicitly or implicitly on *Borak* and its progeny, the courts granted virtually all tender offer participants standing to sue for damages and equitable relief.¹³⁹ Both tendering and non-

§ 240.14a-8 (1990) (shareholder proposal rule)); *cf.* *Rauchman v. Mobil Corp.*, 739 F.2d 205, 207 (6th Cir. 1984) (existence of implied private action under rule 14a-8 assumed but "substantial reservations" expressed).

135 *See, e.g.*, *Greater Iowa Corp. v. McLendon*, 378 F.2d 783 (8th Cir. 1967); *Studebaker Corp. v. Gitlin*, 360 F.2d 692 (2d Cir. 1966).

136 *See, e.g.*, *Union Pac. R.R. v. Chicago & N.W. Ry.*, 226 F. Supp. 400 (N.D. Ill. 1964) (proxy battle between two railroads attempting to take over a third railroad), *cited with approval in* *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 385 (1970); *U.S. Smelting, Ref. & Mining Co. v. Clevite Corp.*, [1969-1970 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 92,691 (N.D. Ohio, June 17, 1968).

137 *See* *Crane Co. v. Westinghouse Air Brake Co.*, 419 F.2d 787, 799-803 (2d Cir. 1969) (assuming standing to sue for damages or equitable relief); *see also* *Lynch v. Fulks*, [1981 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,831 (D. Kan. Dec. 12, 1980) (standing for injunction); *Clayton v. Skelly Oil Co.*, [1977-1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 92,745 (S.D.N.Y. Dec. 30, 1977) (standing for damages).

138 L. LOSS, *supra* note 3, at 944.

139 *See, e.g.*, *Lowenschuss v. Kane*, 520 F.2d 255 (2d Cir. 1975) (standing of tendering shareholder to sue for damages); *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579, 596 (5th Cir.) (standing of nontendering shareholder to sue both individually and derivatively for damages), *cert. denied*, 419 U.S. 873 (1974); *H.K. Porter Co. v. Nicholson File Co.*, 482 F.2d 421 (1st Cir. 1973) (standing of target company and offeror to sue for injunctive relief and damages); *Electronic Specialty Co. v. International Controls Corp.*, 409 F.2d 937 (2d Cir. 1969) (standing of target company to sue for injunctive relief); *McCloskey v. Epko Shoes*, 391 F. Supp. 1279 (E.D. Pa. 1975) (standing of nontendering

tendering shareholders of the target company were found to have standing to sue tender offerors and the target itself. Target companies were accorded standing to sue the offeror, and offerors were granted standing to sue the target and competing offerors. The logic underpinning two-way standing in Williams Act litigation was cogently summarized by the Court of Appeals for the First Circuit:

[I]mplying for the offeror and the target's management reciprocal rights of action for damages seems only fair given that each has a heavy economic stake, and that each is subject to what has been aptly described as "symmetrical" statutory obligations Each is victimized when the other commits illegal acts to defeat or accomplish takeover bids.¹⁴⁰

In the mid-1970s, the transformation from the politically liberal Warren Court to the conservative Burger Court spawned a new judicial philosophy: the role of the federal judiciary should not be expanded and access to the federal courts should be restricted.¹⁴¹ As a manifestation of this philosophy, the Supreme Court shied away from its prior expansive approach to implying private rights of action, becoming less hospitable and at times even hostile.¹⁴² The federal securities laws were not spared. Indeed, the Court not only refused to imply new rights of action under the federal securities statutes but also limited significantly the scope of the implied actions that already existed.¹⁴³ The

shareholder to sue for injunctive relief and damages); *Broder v. Dane*, 384 F. Supp. 1312 (S.D.N.Y. 1974) (standing of tendering shareholder to sue for injunctive relief); see also E. ARANOW, H. EINHORN & G. BERLSTEIN, *DEVELOPMENTS IN TENDER OFFERS FOR CORPORATE CONTROL* 104, 175 n.14 (1977) [hereinafter ARANOW, EINHORN & BERLSTEIN]; Pitt, *supra* note 121, at 131-32.

140 *H.K. Porter Co. v. Nicholson File Co.*, 482 F.2d 421, 424 (1st Cir. 1973) (citation omitted).

141 See Powell, *What the Justices Are Saying . . .*, 62 A.B.A.J. 1454, 1455 (1976). See generally Conard, *Securities Regulation and the Burger Court*, 56 U. COLO. L. REV. 193 (1985) (demonstrating that the transformation in the Court occurred as a result of changes in membership and because some Justices changed sides); Lowenfels, *Recent Supreme Court Decisions Under the Federal Securities Laws: The Pendulum Swings*, 65 GEO. L.J. 891 (1977) (analyzing nine cases in which the author observes the following trends: defendants win, SEC's views rejected, and plaintiffs encouraged to pursue their rights in state rather than federal courts).

142 See Comment, *Implied Rights of Action in Federal Legislation: Harmonization Within the Statutory Scheme*, 1980 DUKE L.J. 928, 928-29. The Court reaffirmed that implied private actions existed under § 14(a) in *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375 (1970), and under rule 10b-5, 17 C.F.R. § 240.10b-5 (1990), in *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972).

143 The Court's restrictive approach to implied private actions during the period

Court's retrenchment was heralded in 1975 by *Cort v. Ash*,¹⁴⁴ a non-securities case, in which the Court articulated a four-pronged test for implying private rights of action from statutes not expressly providing for them. The four factors were as follows:

First, is the plaintiff "one of the class for whose *especial* benefit the statute was enacted"—that is, does the statute create a federal right in favor of the plaintiff? Second, is there any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one? Third, is it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff? And finally, is the cause of action one traditionally relegated to state law, in an area basically the concern of the States, so that it would be inappropriate to infer a cause of action based solely on federal law?¹⁴⁵

As is apparent on its face, the *Cort* test implicitly abandoned *Borak's* effective enforcement theory, and borrowed, in part, from the tort theory used in *Kardon*. The presumption of legislative intent, however, was shifted. Under the tort theory, as indicated above, a private right of action would be implied unless the legislature evidenced a contrary intention. Under *Cort*, a private right of action would be implied only if Congress indicated that such an implication was intended. The test also reflected a change in the Court's view of federal-state relations. In *Borak* and *Bankers Life*, the Court was willing to imply a federal cause of action even

from 1975 to 1977 is exemplified by the following seven cases: Securities Investor Protection Corp. v. Barbour, 421 U.S. 412 (1975) (customers of a broker-dealer member of the Securities Investor Protection Corporation (SIPC) have no implied right of action under the Securities Investor Protection Act of 1970, 15 U.S.C. §§ 78aaa-78111 (1988), to compel the SIPC to perform its duties); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975) (plaintiff claiming an implied action under rule 10b-5, 17 C.F.R. § 240.10b-5 (1990), must be a purchaser or seller of securities); Rondeau v. Mosinee Paper Co., 422 U.S. 49 (1975) (plaintiff must demonstrate irreparable harm to obtain equitable relief in an implied action under § 13(d)); Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976) (scienter is a necessary element in damage suits brought under rule 10b-5); TSC Indus. v. Northway, 426 U.S. 438 (1976) (the standard of "materiality" in implied actions under rule 14a-9, 17 C.F.R. § 240.14a-9 (1990), contemplates a showing by the plaintiff that there was a substantial likelihood that a reasonable shareholder would have considered the omitted fact important in deciding how to vote); Piper v. Chris-Craft Indus., 430 U.S. 1 (1977) (tender offeror has no standing to assert an implied private action for damages under § 14(e)); Santa Fe Indus. v. Green, 430 U.S. 462 (1977) (minority shareholders in a short-form merger cannot recover under rule 10b-5 on the grounds of unfairness or lack of notice).

144 422 U.S. 66 (1975). *Cort* was a unanimous decision, and the opinion was written by Justice Brennan.

145 *Id.* at 78 (citations omitted).

if state law was displaced, whereas in *Cort*, the existence of applicable state law tended to militate against implication. The Court's first occasion to apply its new test in the securities context came in 1977 in a suit brought under the Williams Act, *Piper v. Chris-Craft Industries*.¹⁴⁶

C. The Piper Case

1. Denial of Standing to a Tender Offeror

The litigation in *Piper* involved a contest for control of Piper Aircraft Corporation (Piper) between Chris-Craft Industries, Inc. (Chris-Craft) and Piper's "white knight,"¹⁴⁷ Bangor Punta Corporation (Bangor Punta). The takeover contest, which followed Chris-Craft's successful, hostile cash tender offer for eighteen percent of Piper common stock, centered upon competing exchange tender offers made by Chris-Craft and Bangor Punta. After a hard-fought battle in the marketplace, Bangor Punta emerged the victor, holding over fifty percent—as compared with Chris-Craft's forty-two percent—of the Piper shares.¹⁴⁸ But before Bangor Punta had obtained control, Chris-Craft brought suit under section 14(e) for damages and injunctive relief against the Piper management and Bangor Punta,¹⁴⁹ alleging (1) that the Piper management, in response to Chris-Craft's cash tender offer, issued a misleading press release and sent untrue and misleading letters to Piper shareholders, and (2) that Bangor Punta had filed misleading financial statements with the SEC in connection with its exchange tender offer.¹⁵⁰ The gist of Chris-Craft's claim was that it had been denied a fair opportunity to gain control of Piper by reason of these violations of section 14(e).¹⁵¹ After pro-

146 430 U.S. 1 (1977).

147 A "white knight" is a merger partner or competing offeror that target management finds acceptable.

148 A summary of the takeover contest involved is set forth in *Piper*, 430 U.S. at 4-9.

149 Chris-Craft also sued First Boston Corporation—Piper's investment banker and Bangor Punta's underwriter for its exchange offer. *Id.* at 4-5.

150 Chris-Craft also brought suit against Bangor Punta for damages and injunctive relief under rule 10b-6, 17 C.F.R. § 240.10b-6 (1990). In general, rule 10b-6 prohibits a company whose stock is in the process of distribution from purchasing its stock or rights to purchase its stock until the distribution is finished. *See infra* note 282. Chris-Craft alleged that Bangor Punta made cash purchases of Piper stock during Bangor Punta's exchange offer and that these purchases constituted purchases of Bangor Punta stock rights. *Piper*, 430 U.S. at 7, 9-10.

151 *See Piper*, 430 U.S. at 17 n.14; *id.* at 51 (Blackmun, J., concurring). *But see id.* at 54 (Stevens, J., dissenting) (arguing that Chris-Craft also claimed injury resulting from the

tracted litigation that lasted six years, the Court of Appeals for the Second Circuit held that Chris-Craft had standing to sue under section 14(e), that the defendants had violated section 14(e), and that these violations caused Chris-Craft injury. As a consequence, Chris-Craft was awarded thirty-six million dollars in damages against the defendants (jointly and severally)—the largest amount of damages that had ever been awarded in a securities case¹⁵²—and Bangor Punta was enjoined for five years from voting the Piper shares that it had acquired in its exchange offer in violation of section 14(e).¹⁵³

The Supreme Court accepted the Second Circuit's judgment for certiorari review¹⁵⁴ and reversed, 7-2, in an opinion written by Chief Justice Burger.¹⁵⁵ In addressing only the threshold issue of Chris-Craft's standing, the Court held that a tender offeror, suing *qua* tender offeror, did not have standing to sue for damages under section 14(e).¹⁵⁶ In light of this holding, the Court also vacated the injunction entered against Bangor Punta, concluding that it was based on the impermissible award of damages. In the Court's view, Chris-Craft had explicitly waived any

impairment of the value of its investment in Piper stock).

152 Pitt, *supra* note 121, at 139.

153 The lower court litigation is summarized in *Piper*, 430 U.S. at 9-21. In brief, Chris-Craft first sought a preliminary injunction and it was denied. *Chris-Craft Indus. v. Piper Aircraft Corp.*, 303 F. Supp. 91 (S.D.N.Y. 1969), *aff'd sub nom. Chris-Craft Indus. v. Bangor Punta Corp.*, 426 F.2d 569 (2d Cir. 1970) (en banc). Chris-Craft then sought damages and was successful. The Court of Appeals for the Second Circuit ordered the district court to compute the damages and enjoin Bangor Punta from voting the illegally acquired Piper shares. *Chris-Craft Indus. v. Piper Aircraft Corp.*, 480 F.2d 341 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973). On remand, Chris-Craft was awarded \$1,673,988 plus prejudgment interest, and the injunction was enforced. *Chris-Craft Indus. v. Piper Aircraft Corp.*, 384 F. Supp. 507 (S.D.N.Y. 1974). Chris-Craft then appealed the damages award, and the award was increased substantially. *Chris-Craft Indus. v. Piper Aircraft Corp.*, 516 F.2d 172 (2d Cir. 1975).

154 *Piper v. Chris-Craft Indus.*, 425 U.S. 910 (1976), *granting cert. to* 516 F.2d 172 (2d Cir. 1975).

155 Chief Justice Burger was joined by Justices Stewart, White, Marshall, Powell, and Rehnquist. Justice Blackmun concurred in a separate opinion. Justice Stevens, joined by Justice Brennan, dissented.

156 *Piper*, 430 U.S. at 42 n.28. The Court also held that Chris-Craft did not have standing to sue for damages under rule 10b-6, 17 C.F.R. § 240.10b-6 (1976), because Chris-Craft had alleged injury resulting from a lost opportunity to gain control of Piper and not injury resulting from market tampering at which rule 10b-6 is aimed. *Piper*, 430 U.S. at 42-46.

Justice Blackmun agreed with the dissent that Chris-Craft had an implied private action for damages under § 14(e), but concurred with the majority opinion on the grounds that Chris-Craft had not shown that its injury was caused by the defendants' misconduct. *See id.* at 48 (Blackmun, J., concurring).

independent claim to injunctive relief prior to trial, and the injunction, therefore, had only been granted as an ancillary remedy to accompany the damages award.¹⁵⁷

The Court characterized its holding in *Piper* as a limited one¹⁵⁸ and expressly left open the remaining standing issues under section 14(e)—the standing of target shareholders and the target corporation seeking damages or injunctions,¹⁵⁹ as well as the tender offeror's standing to sue for injunctive relief.¹⁶⁰ Moreover, the Court never confronted the broader question of whether private rights of action could ever be implied under the Williams Act.¹⁶¹ Hence, private suits brought under sections 13(d), 13(e), 14(d), and 14(f) were not specifically foreclosed.

The *Piper* opinion was delivered in two parts, both of which independently sustained the Court's holding. In the first part, the Court restated and then applied the reasoning in *Borak*—a case the Court necessarily found germane since it was the Court's first foray into implying private actions under the federal securities laws. The Court maintained that *Borak* required a two-step inquiry in determining whether a private action should be implied. First, what was the legislative purpose of the statutory provision at issue? And then, was the implication of a private remedy on behalf of the plaintiff necessary to accomplish that purpose?¹⁶² After examining the legislative history of the Williams Act, including numerous statements made during the Act's consideration in Congress, the Court concluded that the "sole purpose" of the Act was the protection of target shareholders. The Court reasoned, there-

157 *Piper*, 430 U.S. at 47. In dissent, Justice Stevens indicated that he was not convinced that Chris-Craft had made a binding election to waive its right to injunctive relief. See *id.* at 70-72 (Stevens, J., dissenting).

158 *Id.* at 42 n.28.

159 *Id.* at 42 n.28, 39 n.25.

160 *Id.* at 47 n.33.

161 *But see id.* at 55 (Stevens, J., dissenting) ("No one seriously questions the premise that Congress implicitly created a private right of action when it enacted § 14(e) in 1968."). It is not clear that the majority opinion would agree with Justice Stevens' statement.

A complete analysis of the implication question could involve a three-step inquiry. First, does the statutory provision involved support implied private actions at all? Second, if so, what parties have standing to assert the private action? And third, what remedies may those parties pursue? See *Sta-Rite Indus. v. Nortek, Inc.*, 494 F. Supp. 358, 360 (E.D. Wis. 1980) (suggesting that some courts, including the Supreme Court, frequently have gone "to the altar" without considering "how they got into the church"); see also *Schneider*, *supra* note 115, at 898-99 (arguing that courts should use the *Cort* test only to answer the first question).

162 See *Piper*, 430 U.S. at 24-26.

fore, that implying a cause of action for damages in favor of a defeated tender offeror was not necessary because tender offerors were not members of the class intended to be protected by the Act.¹⁶³ The SEC, as *amicus curiae*, and Chris-Craft had argued that congressional concern with providing evenhanded protection to all participants in the takeover process was one of the purposes of the Act and, therefore, provided a sufficient basis for conferring standing on a tender offeror.¹⁶⁴ The Court rejected this argument, contending that Congress' policy of neutrality in takeover regulation was merely "one characteristic of legislation directed toward a different purpose—the protection of investors"¹⁶⁵—and that this policy hardly suggested "an intent to confer highly important, new rights upon the class of participants whose activities prompted the legislation in the first instance."¹⁶⁶ Moreover, a denial of standing to a tender offeror under the Act, the Court stressed, was not at odds with *Borak's* grant of standing under section 14(a). The Court explained that the intended beneficiaries of section 14(a) were shareholders—the very class of persons seeking relief in *Borak*—and that *Borak* did not involve the standing of a defeated insurgent group in a proxy battle for corporate control.¹⁶⁷

In the second part of the opinion, the Court applied the four factors that *Cort* had deemed relevant in determining whether a private remedy should be implied on behalf of a particular plaintiff. This analysis, the Court concluded, confirmed its holding that Chris-Craft did not have standing to sue for damages under section 14(e).¹⁶⁸ In considering the first and second factors, the Court observed that its prior examination of the Williams Act clearly demonstrated that Chris-Craft was not an especial beneficiary of the statute, and that there was no evidence that Congress intended to imply a damages remedy in favor of a defeated ten-

163 *Id.* at 26-35.

164 *Id.* at 29. The Court also rejected the argument—which was pressed strenuously by Justice Stevens in dissent—that Chris-Craft was suing not only as a defeated tender offeror but also as a Piper shareholder. *Id.* at 56-59 (Stevens, J., dissenting). The Court reasoned that Chris-Craft's status as a Piper shareholder was nominal since Chris-Craft was not truly in the position of one who was confronted with the decision of whether to tender its stock and that therefore Chris-Craft could be considered only an offeror for purposes of judging its standing to bring a damages suit under § 14(e). *Id.* at 35-36.

165 *Id.* at 29.

166 *Id.* at 30.

167 *Id.* at 33 & n.22.

168 *Id.* at 37.

der offeror.¹⁶⁹ Then, turning to the third factor, the Court asserted that an award of damages to Chris-Craft against Bangor Punta would not be consistent with the statute's purpose—the protection of target shareholders—since the defrauded Piper shareholders who became Bangor Punta shareholders when they accepted the Bangor Punta exchange tender offer would be harmed if a judgment were entered against Bangor Punta.¹⁷⁰ The Court further argued that the threat of damage suits against offerors, rather than protecting target shareholders by deterring violations, might prejudice the shareholders by precluding some offers from ever being made.¹⁷¹ The Court did hint, however, that injunctive actions might be allowed to correct egregious violations of the statute (which the Court believed occurred infrequently), as long as the actions were instituted at an early stage of the takeover contest.¹⁷² With respect to the fourth factor,¹⁷³ the Court focused on the Second Circuit's statement that Chris-Craft's complaint gave rise to a common-law tort claim for interference with a prospective commercial advantage and therefore found that it was appropriate to relegate Chris-Craft to state law to pursue its claim.¹⁷³

2. An Analysis of *Piper*

Piper was a trail marker in the Supreme Court's retreat from expansive notions of standing under the federal securities laws, and it marked the trail in two important respects. First, *Piper* laid the groundwork for the ascendancy of *Cort* over *Borak* in resolving future standing questions in the securities field. Second, the

169 *Id.* at 37-39. Chris-Craft argued that Congress intended tender offerors to have standing under § 14(e) because § 14(e), unlike § 10(b), does not contain the limiting language, "in connection with the purchase or sale of any securities." The Court rejected this argument, claiming that the omission of the purchaser-seller requirement in § 14(e) was only intended to extend anti-fraud protection to nontendering shareholders. *Id.* at 38-39.

170 *Id.* at 39.

171 *Id.* at 39-40. The Court expressed serious reservations whether "deterrence" was a meaningful goal of § 14(e). *Id.* at 40 n.26.

172 *Id.* at 40 n.26; *see id.* at 41-42. Given that Chris-Craft had initially sought, but was denied, an injunction, the Court's suggestion is somewhat ironic. *See supra* note 153. The Court's suggestion also makes one wonder what the Court was thinking when it decided *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49 (1975). *See supra* note 18. In *Rondeau*, the putative target's standing to sue for a *permanent* injunction under § 13(d) was not questioned by the acquirer-defendant and, therefore, was not addressed by the Court. *Id.* at 62.

173 *Piper*, 430 U.S. at 40-41.

Court in *Piper* refused, for the first time, a request to imply a private action under one of the major federal securities statutes.

Even though *Borak* served as the foundation of the *Piper* decision and the *Cort* test was used merely as a confirmation, the *Piper* opinion was purposely designed so that the Court could rely exclusively on *Cort* in future cases. Post-*Piper* Supreme Court decisions corroborate the notion that the Court had this objective in mind, the objective was accomplished in a most adroit way. By construing the *Borak* standard for implying private actions so that it was not dissimilar from the *Cort* test, the Court was able to demonstrate that *Borak* and *Cort* could produce the same result. By making this demonstration at least once, the Court could justify, in subsequent cases, consigning *Borak* to history. There is some question as to whether such action would be necessary if the tests in *Borak* and *Cort* were, in fact, functionally equivalent. But the Court apparently felt that *Borak* had been read too broadly by the lower courts and that it was best to put *Borak* to rest.¹⁷⁴

174 Following closely on the heels of *Piper* were two securities cases in which the Court reaffirmed its reluctance to imply private rights of action. In *Touche Ross & Co. v. Redington*, 442 U.S. 560 (1979), the Court refused to imply a private remedy under § 17(a) of the Exchange Act, 15 U.S.C. § 78q(a) (1988), and in relying heavily on *Cort*'s second factor (legislative intent) stated:

To the extent our analysis in today's decision differs from that of the Court's in *Borak*, it suffices to say that in a series of cases since *Borak* we have adhered to a stricter standard for the implication of private causes of action, and we follow that stricter standard today.

Redington, 442 U.S. at 578. In *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11 (1979), the Court denied an implied remedy under § 206 of the Investment Advisors Act of 1940, 15 U.S.C. § 80b-6 (1988), the general antifraud provision of that statute. The Court, however, did recognize an implied equitable right of rescission under the voidability provision in § 215 of the Act, 15 U.S.C. § 80b-15 (1988).

Implied private actions for damages are not dead. In *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353 (1982), the Court recognized an implied action for damages under the Commodity Exchange Act, 7 U.S.C. §§ 1-26 (1988), analogizing the Act to the federal securities laws. The Court, however, did acknowledge a shift in its approach to implying private actions:

Our approach to the task of determining whether Congress intended to authorize a private cause of action has changed significantly, much as the quality and quantity of federal legislation has undergone significant change. When federal statutes were less comprehensive, the Court applied a relatively simple test to determine the availability of an implied private remedy Under this approach, federal courts, following a common-law tradition, regarded the denial of a remedy as the exception rather than the rule

In 1975 [in *Cort*] the Court unanimously decided to modify its approach to whether a federal statute includes a private right of action.

Id. at 374-77 (footnote omitted). *Cort* is not dead either. In *Daily Income Fund, Inc. v. Fox*, 464 U.S. 523 (1984), the Court, utilizing *Cort*, denied an implied right of action to

Ironically, in paying its last respects to the *Borak* test, the Court gave *Borak* a gloss that may have been originally intended, and moreover, the Court perhaps was correct in indicating that *Borak* can be reconciled with *Cort*. Except for the divergent views expressed in *Borak* and *Cort* regarding the impact of state law on federal implied private actions,¹⁷⁵ *Borak* and *Cort* were not in competition with each other. The analytical focus of the test in *Cort* was certainly statutory purpose. Although a major thrust of *Borak* was that private enforcement of the SEC's rules provided a necessary supplement to SEC action, the Court never claimed that the SEC's inability to pursue all proxy violations was a sufficient justification for granting every party interested in a proxy contest a right to sue.¹⁷⁶ Rather, *Borak* implied a private action in favor of a shareholder under the proxy rules because shareholder enforcement served one of the purposes of section 14(a). Thus, fairly read, *Borak*, like *Cort*, focused on statutory purpose as the ultimate touchstone.

(a) *Statutory Objectives as Evidence of Legislative Intent.*—Even if the Court's harmonization of *Borak* with *Cort* was strained, *Piper*'s reliance on statutory purpose was nonetheless sound. Because the legislative history of the Williams Act contains no explicit indication whether Congress intended a court to read a private action into the Act, discerning the statute's goals could reveal what Congress implicitly intended. Presumably, Congress intended a court to create a private remedy if a statutory purpose were likely to be frustrated absent private enforcement. In reviewing the legislative materials to divine the Act's purposes, the Court was cast adrift, however, by adopting a narrow view of what constituted a statutory purpose. As a consequence, the Court's analysis was fundamentally flawed.

In the main, the holding in *Piper* hinged on the Court's conclusion that the legislative history of the Williams Act evinced only one statutory purpose—the protection of target shareholders through full and fair disclosure of information—and that Congress' desire to attain neutrality in the regulation of tender offers was a statutory *policy* and not a statutory *purpose*.¹⁷⁷ In

an investment company under § 36(b) of the Investment Company Act of 1940, 15 U.S.C. § 80a-35(b) (1988). *Id.* at 541.

175 See *infra* text preceding note 191.

176 See *Piper*, 430 U.S. at 41.

177 *But cf.* *Edgar v. MITE Corp.*, 457 U.S. 624, 633 (1982) (plurality opinion) ("There

Borak, the Court asserted that the protection of investors was "among [section 14(a)'s] chief purposes,"¹⁷⁸ and therefore it would be odd if the protection of target shareholders were the sole purpose of the Williams Act.¹⁷⁹ Thus, whether neutrality is called a purpose or a policy would seem to be largely a matter of semantics, but for the *Piper* Court it was a distinction of no small significance. According to the Court, reliable inferences about the legislative intent could be drawn from a statutory purpose, but a statutory policy was nonprobative. By taking this stance as to what was relevant, the Court failed to come to grips with the legislative history pertaining to Congress' concern with neutrality—legislative history that sheds significant light on whether Congress intended a court to infer a private action from the statute.¹⁸⁰

As explained in Part I of the Article, when Congress passed the Williams Act, it had a strong commitment to maintaining neutrality between tender offerors and target corporations. This commitment permeates the legislative history and the statutory provisions themselves.¹⁸¹ As the legislative history makes abundantly clear, neutrality was achieved by two regulatory techniques that were designed to serve target shareholders, the intended

is no question that . . . Congress intended to protect investors. But it is also crystal clear that a major aspect of the effort to protect the investor was to avoid favoring either management or the takeover bidder." (citations omitted)); *Data Probe Acquisition Corp. v. Datatab, Inc.*, 568 F. Supp. 1538, 1545 (S.D.N.Y.) (stating in a section of the opinion entitled "Dual Purposes of the Williams Act," that "[the Court's decision in *MITE*] reveals that important aspects of the legislative history of the Williams Act had not been fully examined in [*Piper*]"), *rev'd*, 722 F.2d 1 (2d Cir. 1983), *cert. denied*, 465 U.S. 1052 (1984); Note, *Fear of the Hostile Takeover: Having Tamed and Reined the Beasts, State Regulation Would Kill Them As Well*, 14 J. CORP. L. 133, 152 (1988) ("[Post-*Piper*] cases and commentary led to the conclusion that the goal of neutrality carries equal weight with the goal of shareholder protection."); *see also supra* note 53.

178 *Borak*, 377 U.S. at 432.

179 Even in *Cort*, 442 U.S. at 78, the Court concluded that the plaintiff is "one of the class for whose *especial* benefit the statute was enacted" (first factor), when there is generally a "pervasive legislative scheme governing the relationship between the plaintiff class and the defendant class in a particular regard." *Id.* at 82. A tender offeror would clearly seem to meet this test; the Court, however, never mentioned it. This aspect of the first factor in *Cort* would have certainly militated in favor of Chris-Craft's standing to sue under § 14(e).

180 The Court did review portions of the legislative materials that had a bearing on Congress' concern with neutrality, but the materials it chose were not representative. *See Pitt, supra* note 121, at 141, 166 (maintaining that the Court reviewed "carefully selected" and "isolated" portions of the legislative history); *see also* Karjala, *Federalism, Full Disclosure, and the National Markets in the Interpretation of Federal Securities Laws*, 80 NW. U.L. REV. 1473, 1495 (1986) ("The legislative history of the Williams Act is rich and amenable to more than one interpretation.").

181 *See supra* note 51; *see also supra* text accompanying notes 42-53, 79-82, 89-109.

beneficiaries of the statute, in two interrelated ways. First, Congress imposed disclosure obligations on both offerors and targets for the *protection* of target shareholders. With balanced disclosure, target shareholders would be able to make an informed choice because they would have the necessary information from both sides of the contest. Second, Congress regulated the conduct of both offerors and targets for the *benefit* of target shareholders. With evenhanded regulation, target shareholders would not be deprived of the opportunity to make a choice in the first place because potential offerors would not be discouraged from making a bid. Thus, for Congress, neutrality meant not only enhanced disclosure protections for target shareholders but also preservation of the tender offer as a viable means for target shareholders to displace management and receive a premium for their shares.

The critical inquiry, therefore, is whether a denial of standing to a tender offeror seeking money damages frustrates Congress' commitment to preserving the viability of the tender offer process. The Court in *Piper* contended that if standing were granted, the constant threat of damage suits would deter some offers from ever being made.¹⁸² Much more likely is the prospect that would-be offerors will be discouraged from making bids if they are powerless to compensate themselves for injury suffered as a result of the foul play of their opponents.¹⁸³ Furthermore, after *Piper*, offerors cannot even be assured of an implied injunctive

182 *Piper*, 430 U.S. at 38-39; see *supra* note 171. The opinion reflects an overall abhorrence of massive damages awards in tender offer litigation, particularly when the award does not redound to the benefit of the target shareholders. *Piper*, 430 U.S. at 39. In this regard, it is noteworthy that when the amount of damages had not yet been determined, the Court denied Bangor Punta's petition for a writ of certiorari. *Piper v. Chris-Craft Indus.*, 414 U.S. 910, *denying cert. to* 480 F.2d 341 (2d Cir. 1973); see *supra* note 153.

Also, the Court correctly pointed out that some *Piper* shareholders would be harmed by an award of damages to Chris-Craft against Bangor Punta. See *supra* text accompanying note 170. Injury to tendering shareholders would only occur, however, in an exchange tender offer. In a cash tender offer—the primary focus of Congress' attention when it embarked on tender offer legislation—tendering shareholders would not be harmed by a damages award against the successful contestant because they have tendered for cash not securities. (At the time of the Bangor Punta exchange offer (1969), none of the Williams Act provisions, except § 14(e), applied to exchange offers. See *supra* note 55.) Furthermore, as Justice Stevens indicated in dissent, the judiciary should be able to structure a remedy to avoid harm to tendering shareholders in an exchange offer. *Piper*, 430 U.S. at 69 (Stevens, J., dissenting).

183 Although it is not clear why Chris-Craft withdrew from the contest for control of *Piper* when it did, see *Piper*, 430 U.S. at 9 n.7, it would seem that Chris-Craft realized that shifting the battle to the courtroom was a more profitable course to follow. See Pitt, *supra* note 121, at 136.

action to correct or remedy the wrongdoings of their opponents. Although the Court did suggest that injunctive relief may be available to redress violations of section 14(e), it emphasized the likely conditions of availability—the violations would have to be flagrant and detected at an early stage of the contest—and it never stipulated that an offeror would be the proper party to seek such relief.¹⁸⁴ And at least conceptually, there is good reason to conclude that the Court did not intend to extend even this narrowly circumscribed right to offerors. A Congress that did not focus on implied actions at all surely did not differentiate between damages and injunctions. Therefore, since the Court held that Congress did not intend to confer standing upon an offeror to maintain a damages action, it seems that the Court would have also concluded that Congress did not intend an offeror to have standing to pursue injunctive relief. In light of these considerations, a denial of standing to a tender offeror seeking damages, in the long run, may impair the vigor of the tender offer process, depriving target shareholders of the benefit Congress intended—the opportunity to make a choice. If this view proves to be accurate, Congress' commitment to neutrality furnishes an independent basis for allowing a tender offeror to sue for damages under section 14(e).

Congress' commitment to neutrality, however, provides a more compelling basis for resolving the standing issue in *Piper*. If target shareholders are the only intended beneficiaries of the Williams Act, they should have standing to sue individually and derivatively to redress violations of that Act. Given the obvious parallel between proxy and tender offer regulation, this proposition is dictated by *Borak's* holding,¹⁸⁵ which was undeniably left intact in *Piper*.¹⁸⁶ If a target shareholder can sue derivatively, then a target corporation should be able to assert remedies on behalf of its shareholders as a group. Further, once a target is given standing under the Act, it ineluctably follows that a tender

184 *Piper*, 430 U.S. at 40 & n.26, 41-42. Furthermore, even though the issue was not raised in the petitions for certiorari, the Court took the initiative in vacating the district court's entry of the injunction barring Bangor Punta from voting its Piper stock. Justice Stevens felt the Court had been officious in this regard. He contended in dissent that "[t]he injunction was an independent remedy premised on the violations of law found by the lower courts. Setting aside the damages recovery provides an *additional* reason for permitting the injunction to remain in effect" *Id.* at 70 (Stevens, J., dissenting).

185 See *supra* text accompanying note 132.

186 Subsequent to its *Piper* decision, the Court clarified that *Borak* has been grandfathered. See *Touche Ross & Co. v. Redington*, 442 U.S. 560, 577 (1979) ("[W]e do not now question the actual holding of *Borak* . . .").

offeror should have similar standing, or the neutral balance Congress sought to effect will be tipped in favor of target management.¹⁸⁷ The *Piper* Court presumably realized that this concatenation of implications existed, and that is why the Court refused to intimate its views on the first two links in the chain (the standing of target shareholders and the target company) and downplayed Congress' concern with neutrality.

(b) *Contemporary Legal Context as Evidence of Legislative Intent.*—Drawing inferences from statutory purposes is not the only way of determining legislative intent. As the second factor in *Cort* recognizes, there may be other evidence indicating that Congress intended to create or deny an implied remedy. The Court, however, gave short shrift to this factor. Having found that target shareholders were the sole beneficiaries of the statute, the Court concluded, in effect, that Congress must have intended to deny a damages remedy to tender offerors. A more probing analysis would have revealed that the contemporary legal context in which Congress passed the Williams Act strongly suggests that Congress intended all tender offer participants to have standing to sue for damages and injunctions to redress violations of the Act.¹⁸⁸ As indicated above, prior to the adoption of the Williams Act, the lower courts, following *Borak's* lead, had construed the proxy rules to permit implied damages and injunctive actions brought at the behest of all parties involved in a proxy contest—sharehold-

187 *But cf. The Supreme Court, 1976 Term—Leading Cases*, 91 HARV. L. REV. 70, 79 n.35 (1977) (suggesting that the congressional policy of neutrality should mean that neither tender offerors nor target corporations have standing to sue and that the Court will have to overrule that part of *Borak* which permitted shareholders to sue derivatively under § 14(a) if neutrality is to be maintained).

188 See *Cannon v. University of Chicago*, 441 U.S. 677 (1979) (utilizing the *Cort* factors and the "contemporary legal context" to find that a private right of action was implicit in § 901(a) of Title IX of the Education Amendments of 1972, 20 U.S.C. § 1681(a) (1988); *Howing Co. v. Nationwide Corp.*, 826 F.2d 1740 (6th Cir. 1987) (employing the same approach to create a private right of action for damages under § 13(e) of the Williams Act).

In one major respect, the Williams Act has a greater claim to implied private actions than either § 14(a) or § 10(b). In 1934, Congress may not have enacted §§ 14(a) and 10(b) with the understanding that the judiciary would allow private parties to sue under these provisions. See 2 L. LOSS, SECURITIES REGULATION 942 (2d ed. 1961); cf. Kitch, *A Federal Vision of the Securities Laws*, 70 VA. L. REV. 857, 863, 866 (1984) (contending that "Kardon . . . was a fluke" and that "Borak was an indefensible construction of the statute"). In 1968, however, Congress probably did pass the Williams Act believing that the judiciary would permit implied private suits under the Act since the courts had permitted such suits under §§ 14(a) and 10(b).

ers, management, and outsiders seeking control.¹⁸⁹ By consciously choosing to pattern the Williams Act after the proxy provisions, Congress presumably was aware of this decisional law and intended the Williams Act to be interpreted in conformity with it. Furthermore, by the time of the 1970 amendments to the Williams Act, the lower courts had already assumed that shareholders, targets, and tender offerors had standing to sue under the Act. Congress' failure to repudiate this case law in the 1970 amendments indicates implicit approval.¹⁹⁰

(c) *State Law as Evidence of Legislative Intent.*— The Supreme Court has never flatly acknowledged that there was a significant point of divergence between *Borak* and *Cort* on the relevance of state law in determining whether Congress intended to create a federal implied remedy. As described above, *Borak* contended that state law was generally inapposite; *Cort* (by dint of the fourth factor in its test) maintained that the existence of a state-law remedy for a cause of action—to the extent that the action was traditionally relegated to state law, in an area of basic concern to the states—indicated that Congress may not have intended to create a similar federal remedy.¹⁹¹ The opinion in *Cort* did assert, however, that had its fourth factor been used in *Borak*, the holding would not have been altered. The Court explained: “In *Borak*, the statute involved was clearly an intrusion of federal law into the internal affairs of corporations; to the extent that state law differed or impeded suit, the congressional intent could be compromised in state-created causes of action.”¹⁹²

189 See *supra* text accompanying notes 134-38.

190 See Conard, *supra* note 141, at 215-16 & n.150 (finding it curious that the “major” amendments to the securities laws, such as the amendments to the Williams Act, were not considered when the Court rejected implied private actions in securities cases).

191 The fourth factor in *Cort*, like the other factors, is not dispositive of the question whether Congress intended to provide a similar federal remedy but merely one indicator of what Congress may have intended. See *Santa Fe Indus. v. Green*, 430 U.S. 462, 478 (1977); see also *Touche Ross & Co. v. Redington*, 442 U.S. 560, 575 (1979) (“[T]he Court [in *Cort*] did not decide that each of [the four factors] is entitled to equal weight.”).

192 *Cort*, 422 U.S. at 85. Either side in a proxy contest may choose to challenge an election on several grounds. Some of these grounds involve solely questions of state law: forged proxies, improperly signed proxies, proxies given by shareholders who are not holders of record, or proxies revoked by subsequent proxies. Other grounds implicate solely questions of federal law: oral or written solicitation without furnishing a proxy statement (in violation of rule 14a-3(a), 17 C.F.R. § 240.14a-3(a) (1990)) or solicitation by an opposition group of more than 10 persons without filing a proxy statement with the SEC (see rule 14a-2(b)(1), *id.* § 240.14a-2(b)(1)). And one ground involves questions of both federal and state law: solicitation on the basis of misleading information in viola-

This sound explanation draws attention to the serious shortcomings in *Piper's* analysis of a comparable issue. It will be recalled that the *Piper* Court concluded, without discussion, that because Chris-Craft had a colorable claim under state law for interference with a prospective advantage, deference to state law was appropriate.¹⁹³ Had the Court evaluated, as *Cort* requires, the state interest involved, the Court would have reached a different conclusion. At the time the Williams Act was adopted, misconduct in connection with tender offers was not specifically governed by state law, and tender offer regulation was not a major concern of the states.¹⁹⁴ Furthermore, the state common law of deceit has not prevented the federal courts from implying private actions under rule 10b-5 on behalf of defrauded buyers and sellers of securities.¹⁹⁵ More important, if state remedies are inadequate to redress federal proxy violations, they should also be inadequate to redress federal tender offer violations. After all, the Williams Act, like proxy regulation, is an intentional and permissible intrusion by Congress into state corporation law.¹⁹⁶ In short, Congress intended federal law to remedy violations of the Williams Act, and it viewed available state law remedies as merely supplemental.

The *Piper* Court was forced, of course, to give summary treatment to the fourth factor in the *Cort* test, since a complete analysis would have cast doubt on its earlier conclusion that Chris-Craft was not entitled to sue. But the summary treatment was not just expedient. It enabled the Court to espouse an even greater deference to state law than *Cort*.¹⁹⁷ And the deference to state law in *Piper* epitomizes the Burger Court's view of the proper relationship between federal and state law in remedying violations of the federal securities laws—a view that is diametrically opposite from that taken by the Warren Court in *Borak*.

tion of rule 14a-9, *id.* § 240.14a-9. See L. LOSS, *supra* note 3, at 949-50.

193 See *supra* text accompanying note 173.

194 See Pitt, *supra* note 121, at 171-72; see also *supra* note 38.

195 See *supra* text accompanying note 125.

196 See, e.g., *supra* text following notes 88 & 95; *supra* text accompanying note 109.

197 See Anderson, *The Meaning of Federalism: Interpreting the Securities Exchange Act of 1934*, 70 VA. L. REV. 813, 829 (1984) (maintaining that the Burger Court had a "preference for state law over federal law" and that "[u]sing notions of federalism to construct a particular view of congressional intent provide[d] a way of giving effect to such a preference while disguising it as a kind of neutral principle of statutory interpretation").

(d) *Some Concluding Remarks on Piper.*—For a decision that purports to be a studious attempt to reconstruct the intent of the Williams Act Congress, *Piper* missed the mark considerably. Indeed, the preceding analysis of the *Piper* case has adduced three indicants of legislative intent—Congress' commitment to neutrality in the regulation of tender offers, the contemporary legal context in which the Williams Act was adopted, and Congress' deliberate decision to intrude into state corporation law by passing tender offer legislation—which all point to the conclusion that Congress intended tender offerors to be able to sue for damages under section 14(e). And what is more, this evidence of legislative intent supports an even broader conclusion: Congress intended *all* tender offer participants—target shareholders, target corporations, and tender offerors—to have standing to sue for *all* necessary relief, whether it be damages or equitable remedies, to redress violations of *all* provisions of the Williams Act.

In light of this conclusion, the best explanation for the holding in *Piper* is that the Court wanted to give Congress an unmistakable message: be explicit when federal remedies are intended, or the Court is going to bow to state law.¹⁹⁸ There is nothing inherently troublesome about instructing Congress how to accomplish its task more effectively, but when the instruction eviscerates what Congress has done while it was not so well schooled, then it is unfair. When Congress passed the Williams Act, it had every reason to believe that the courts would imply private actions under the statute and work out the nuances of each cause of action.¹⁹⁹ The courts, including the Supreme Court, had done so

198 Two years later, the Court was much more explicit in this regard. See *Cannon v. University of Chicago*, 441 U.S. 677, 717 (1979) ("When Congress intends private litigants to have a cause of action to support their statutory rights, the far better course is for it to specify as much when it creates those rights."); see also *id.* at 718 (Rehnquist, J., concurring) ("[T]his Court in the future should be extremely reluctant to imply a cause of action absent . . . specificity on the part of the Legislative Branch.").

199 Professor Conard has cogently evaluated the implication issue as follows:

There is not much merit in the argument that if Congress had wanted fraud victims to have rights of action, it would have given them express rights. Congress did grant express rights of action where it could feasibly define the offense and prescribe appropriate elements of proof, measures of damages, and periods of limitations. But the general fraud prohibitions comprise transactions that the legislators had not yet visualized If there were legislators or draftsmen who thought about the advisability of prescribing private actions for some of the unspecified frauds covered by these prohibitions, they would probably have chosen to rely on courts to entertain private actions appropriate to the

before without any express congressional directive.²⁰⁰ Why would they stop now? The Williams Act Congress, however, did give the courts two meaningful signals. By incorporating the Williams Act into the Exchange Act—legislation that was predicated on principles of deterrence and compensation²⁰¹—Congress signalled that the Williams Act had these same roots. Also, by crafting the Williams Act to provide evenhanded *regulatory* protection for all tender offer participants, Congress signalled that the Courts should fashion evenhanded *remedial* protection. And the courts read and heeded these signals for almost a decade.

D. *Standing to Sue Under the Williams Act After Piper*

Piper certainly gave the courts a much different signal: standing to sue under the Williams Act was no longer to be routinely granted. And as Senator Williams declared shortly after the *Piper* decision was handed down: “[*Piper*] may have substantially changed the contours of litigation under the tender offer statutes in a manner never intended or envisioned by the Congress.”²⁰² But because a substantial majority of the courts have read *Piper* narrowly, the decision has not turned out to be as ominous as Senator Williams predicted. In general, target shareholders have been granted standing to sue for both damages and injunctions.²⁰³

various offenses, in the manner that had been approved by the Supreme Court before the securities laws were adopted.

Conard, *supra* note 141, at 220.

200 The Court in *Cannon*, 441 U.S. 677 (1979), did recognize that the legislative history of a statute which does not expressly create or deny a remedy will usually be silent or ambiguous. *See id.* at 694.

201 *See Pitt, supra* note 121, at 162-63.

202 Williams, *Introduction to ARANOW, EINHORN & BERLSTEIN, supra* note 139, at xviii (1977) (emphasis added).

203 *See, e.g., Polaroid Corp. v. Disney*, 862 F.2d 987 (3d Cir. 1988) (suggesting that an injunctive action may be available under rule 14d-10, 17 C.F.R. § 240.14d-10 (1990)); *Field v. Trump*, 850 F.2d 938 (2d Cir. 1988), *cert. denied*, 489 U.S. 1012 (1989); *Howing Co. v. Nationwide Corp.*, 826 F.2d 1470 (6th Cir.) (damages action under § 13(e)), *cert. denied*, 468 U.S. 1059 (1987); *Pryor v. United States Steel Corp.*, 794 F.2d 52 (2d Cir.) (damages action under § 14(d)), *cert. denied*, 479 U.S. 954 (1986); *Plaine v. McCabe*, 797 F.2d 713 (9th Cir. 1986) (damages action under § 14(e)); *Schlesinger Inv. Partnership v. Fluor Corp.*, 671 F.2d 739 (2d Cir. 1982) (same); *Osofsky v. Zipf*, 645 F.2d 107 (2d Cir. 1981) (same); *Caleb & Co. v. E.I. duPont Nemours & Co.*, 615 F. Supp. 96 (S.D.N.Y. 1985) (same); *Bolton v. Gramlich*, 540 F. Supp. 822 (S.D.N.Y. 1982) (ruling that tender offerors, as shareholders, can sue derivatively under § 14(e) for damages and injunctive relief); *American Bakeries Co. v. Pro-Met Trading Co.*, [1981 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,925 (N.D. Ill. Mar. 27, 1981) (suggesting that an injunctive action may be available under § 13(d)). Tendering shareholders may not need § 14(e) because they are sellers within rule 10b-5, 17 C.F.R. § 240.10b-5 (1990).

Since *Piper* ruled that the Act was passed for the "special benefit" of the target shareholders, the courts have reasoned that target shareholders should have a private right of action.²⁰⁴ Next, the courts have indicated that suits brought by target companies for damages are no longer permissible because they destroy the neutrality Congress sought to achieve.²⁰⁵ And finally, although there are some maverick cases denying targets and offerors the right to sue for injunctive relief,²⁰⁶ it seems to be generally accepted that such relief is available.²⁰⁷ The courts have realized that targets and offerors, more than anyone else, have the necessary incentive and the best resources to correct violations of the Act.

When target corporations or tender offerors are denied standing to sue under the Williams Act, they have no choice but to lean on applicable state common-law remedies. Defeated tender offerors may have a claim, as in *Piper*, for interference with a

204 Compare *Kalmanovitz v. G. Heileman Brewing Co.*, 769 F.2d 152, 159, 160 (3d Cir. 1985) (indicating that the proposition advanced by the text "arguably may be correct" but holding that after *Piper* (see *supra* note 164) "a plaintiff who occupies the dual roles of a very substantial tender offeror and merely a nominal target shareholder may be considered to be only an offeror for purposes of judging standing") with *Shamrock Holdings, Inc. v. Polaroid Corp.*, 709 F. Supp. 1311, 1317 n.7 (D. Del. 1989) (large target shareholder has standing to sue even though it is also the offeror).

205 See, e.g., *Wellman v. Dickinson*, 475 F. Supp. 783, 816 (S.D.N.Y.) (1979) (dictum) ("[I]t now seems clear that a target company . . . lacks standing to bring a damage action . . . for violations of Sections 14(d) and 14(e) of the Williams Act."), *aff'd*, 682 F.2d 355 (2d Cir. 1982), *cert. denied*, 460 U.S. 1069 (1983). In general, the courts have refused to imply a right of action for damages on behalf of target companies (or their shareholders) under § 13(d) both before and after *Piper*. See, e.g., *Myers v. American Leisure Time Enters.*, 402 F. Supp. 213 (S.D.N.Y. 1975) (derivative and class action), *aff'd without opinion*, 538 F.2d 312 (2d Cir. 1976); *Kirsch Co. v. Bliss & Laughlin Indus.*, 495 F. Supp. 488 (W.D. Mich. 1980) (dictum).

206 See, e.g., *Liberty Nat'l Ins. Holding Co. v. Charter Co.*, 734 F.2d 545 (11th Cir. 1984) (ruling that there was no private right of action for injunctive relief (divestment of shares) in favor of a target company under §§ 13(d), 14(d), or 14(e)); *Kalmanovitz v. G. Heileman Brewing Co.*, 769 F.2d 152 (3d Cir. 1985) (ruling that there was no private right of action for injunctive relief in favor of a tender offeror under §§ 13(e), 14(d), or 14(e)).

207 See, e.g., *Florida Commercial Banks v. Culverhouse*, 772 F.2d 1513 (11th Cir. 1985) (ruling that its earlier decision in *Liberty National* (see *supra* note 206) did not preclude a target company from seeking corrective relief under §§ 13(d), 14(d), or 14(e)); *Indiana Nat'l Corp. v. Rich*, 712 F.2d 1180 (7th Cir. 1983) (ruling that a target company has standing to sue for injunctive relief under § 13(d)); *Buffalo Forge Co. v. Ampco-Pittsburg Corp.*, 638 F.2d 568 (2d Cir. 1981) (assuming, without discussion, that a target company has standing to sue for injunctive relief under § 14(d)); *Prudent Real Estate Trust v. Johncamp Realty*, 599 F.2d 1140 (2d Cir. 1979) (ruling that a target company has standing to sue for injunctive relief under § 14(e)); *Mobil Corp. v. Marathon Oil Corp.*, 669 F.2d 366 (6th Cir. 1981) (ruling that a tender offeror has standing to sue for injunctive relief under § 14(e)), *cert. denied*, 455 U.S. 982 (1982); *Humana, Inc. v. American Medicorp, Inc.*, 445 F. Supp. 613 (S.D.N.Y. 1977) (same).

prospective advantage, and target corporations may plausibly be able to pursue an action in deceit on behalf of defrauded shareholders.²⁰⁸ These two common-law tort actions are usually perceived, however, to be ineffectual or inadequate,²⁰⁹ and as a result, they have been seldom used in tender offer litigation.²¹⁰ Asserting a claim under one of the state takeover statutes, which may even have an antifraud provision that parallels section 14(e),²¹¹ is not a viable alternative, because these statutes do not support private actions²¹² or liability runs only in favor of target shareholders.²¹³

What has been said thus far displays the patent inconsistency that exists today, at least on the books, in the remedial aspects of proxy and tender offer regulation. When a claim for damages is at issue, both sides of a proxy contest have standing to sue under federal law, whereas tender offerors and target corporations are relegated to state law to pursue their claims. Although the Supreme Court in *Piper* expressly declined to indicate whether an insurgent group in a proxy contest has standing to sue for damages, it seems that the Court would have denied standing to both

208 See Comment, *An Implied Private Right of Action Under the Williams Act: Tradition vs. Economic Reality*, 77 NW. U.L. REV. 316, 346 (1982). Also, target shareholders may have a state-law cause of action against target management for interference with a prospective advantage, see *infra* note 210, or breach of fiduciary duty on the grounds that management defended against a tender offer solely to retain control, see ARANOW, EINHORN & BERLSTEIN, *supra* note 139, at 116; McIntyre, *Shareholders' Recourse Under Federal Securities Laws Against Management for Opposing Advantageous Tender Offers*, 34 BUS. LAW. 1283, 1289-90 (1979).

209 See Pitt, *supra* note 121, at 119 n.7. Chris-Craft sued Piper and Bangor Punta in state court for interference with a prospective advantage, and the suit was ultimately settled when Chris-Craft agreed to sell its Piper shares to Bangor Punta at \$70 a share. See Note, *Corporate Takeover Statutes and the Defeated Offeror: The Aftermath of Piper*, 9 U. TOL. L. REV. 95, 104 n.35 (1977).

210 See Lowenstein, *Tender Offer Litigation and State Law*, 63 N.C.L. REV. 493, 495-97 (1985) (citing cases in which a defeated offeror or target shareholder has sought damages or injunctive relief for interference with a prospective advantage and maintaining that relief is possible but only after significant difficulties are overcome). See generally Walker, *Restitutionary Relief in the Absence of Standing to Challenge Violations of Rule 10b-5 and Section 14(e)*, 23 LOY. L. REV. 893 (1977) (suggesting that the common-law remedy of restitution may be the panacea for parties who are denied standing to sue under § 14(e)).

211 See Note, *Securities Law: Implied Causes of Action Under Section 14(e) of the Williams Act*, 66 MINN. L. REV. 865, 868 n.16 (1982) (listing 27 state takeover statutes (as of 1981) that contain antifraud provisions patterned after § 14(e)).

212 Cf. *Philbosian v. First Fin. Sec. Corp.*, 550 F. Supp. 210 (D. Colo. 1982) (holding that there is no private right of action under the general anti-fraud provision of the Colorado securities statute, COLO. REV. STAT. § 11-51-123 (1987)).

213 See, e.g., MASS. GEN. L. ch. 110C, § 9 (Law. Co-op. 1985).

insurgents and the corporation had the question been raised. The standing of proxy contestants has not arisen in the post-*Piper* era, mainly because most contests for corporate control have been waged via tender offers. There have been lower court decisions construing the proxy rules, however, and this case law reflects a manifest unwillingness to retreat from the expansive interpretations of the proxy rules that had characterized the pre-*Piper* era.²¹⁴ Furthermore, courts continue to cite *Borak* in proxy cases, and they correctly assert that the Supreme Court has never restricted the class of potential plaintiffs that can sue under section 14(a).²¹⁵ While the inconsistency in proxy and tender offer regulation must await a definitive pronouncement by the Court, it is not unlikely that the lower courts will retain two-way standing in proxy contests in future cases. And more proxy contest litigation is bound to surface, since in the past few years the market for corporate control has seen a rejuvenation of proxy contests as a takeover technique, and these contests are being waged with increasing frequency in connection with tender offers.²¹⁶ In this context, incongruous standing rules will prove to be most blatant. The developments in this area are worth watching.

III. THE SUBSTANTIVE COVERAGE OF THE WILLIAMS ACT

A. *The Scope of Section 14(e) Before Schreiber*

As the number and size of tender offers increased in the years after the Williams Act was adopted,²¹⁷ the tactics employed by tender offerors and target companies to promote and defeat tender offers became more sophisticated and complex.²¹⁸ One of the most significant legal developments that accompanied this trend was the proliferation of lawsuits instituted by offerors under section 14(e) of the Williams Act to enjoin the defensive arrangements of targets.²¹⁹ The courts that were called upon to

214 See, e.g., *Cowin v. Bresler*, 741 F.2d 410 (D.C. Cir. 1984); *Lynch v. Fulks*, [1981 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,831 (D. Kan. Dec. 12, 1980). *Contra* *Bolton v. Gramlick*, 540 F. Supp. 822 (S.D.N.Y. 1982). See generally 2 T. HAZEN, *supra* note 56, § 13.1, at 56 (arguing that while the Supreme Court is becoming more restrictive in applying the *Cort* test, the lower courts in securities cases seem to be taking a contrary approach).

215 See, e.g., *Cowin v. Bresler*, 741 F.2d 410, 426 (D.C. Cir. 1984).

216 See L. LOSS, *supra* note 3, at 499 n.5.

217 See MERRILL LYNCH BUSINESS BROKERAGE & VALUATION (W.T. Grimm & Co.), 1988 MERGERSTAT REVIEW 7, 85 (1989), 1989 MERGERSTAT REVIEW 7, 75 (1990).

218 See generally 1 A. FLEISCHER, TENDER OFFERS: DEFENSES, RESPONSES, AND PLANNING 391-612 (2d ed. 1983) (case studies).

219 Although bidders usually prefer to avoid litigation, they sometimes are forced to

rule in these cases assumed that the offerors had standing to sue for such relief—both before and after *Piper*²²⁰—and initially the courts were receptive to the underlying claims as well.²²¹ In general, the initial decisions held that the directors' adoption of a defensive measure for no justifiable business purpose was a breach of the directors' fiduciary duty owed to the target shareholders under state law and that this fiduciary misconduct constituted a violation of section 14(e)'s second prong outlawing "fraudulent, deceptive, or manipulative acts or practices in connection with any tender offer."²²² The defenses that foundered in these law-

use the courts when the target's defensive measures are particularly potent. *See id.* at 297-98. Target litigation, however, is common. Indeed, almost whenever a hostile tender offer is launched, the target dashes to the courthouse, intent on charging the offeror with every impropriety that counsel can muster. *See, e.g.,* ARANOW, EINHORN & BERLSTEIN, *supra* note 139, at 199-202; *see also supra* note 94. *See generally* Rosenzweig, *Target Litigation*, 85 MICH. L. REV. 110 (1986) (arguing that target managers sue bidders in order to thwart hostile takeovers and that they often succeed). Judge Friendly described the inevitable stream of litigation from a hostile tender offer in this way:

Drawing Excalibur from a scabbard where it would doubtless have remained sheathed in the face of a friendly [tender] offer, the target company typically hopes to obtain a temporary injunction which may frustrate the acquisition since the offering company may well decline the expensive gambit of a trial or, if it persists, the long lapse of time could so change conditions that the offer will fail even if, after a full trial and appeal, it should be determined that no . . . violation has been shown.

Missouri Portland Cement Co. v. Cargill, Inc., 498 F.2d 851, 854 (2d Cir.), *cert. denied*, 419 U.S. 883 (1974).

220 *See, e.g.,* Mobil Corp. v. Marathon Oil Co., 669 F.2d 366, 370-73 (6th Cir. 1981), *cert. denied*, 455 U.S. 982 (1982); Data Probe Acquisition Corp. v. Datatab, Inc., 568 F. Supp. 1538, 1544 n.1 (S.D.N.Y.), *rev'd on other grounds*, 722 F.2d 1 (2d Cir. 1983), *cert. denied*, 465 U.S. 1052 (1984); Buffalo Forge Co. v. Ogden Corp., 555 F. Supp. 892, *aff'd*, 717 F.2d 757 (2d Cir.), *cert. denied*, 464 U.S. 1018 (1983); Applied Digital Data Sys. v. Milgo Elec. Corp., 425 F. Supp. 1145 (S.D.N.Y. 1977); Royal Indus. v. Monogram Indus., [1976-1977 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,863 (C.D. Cal. Nov. 29, 1976); Orbanco, Inc. v. Security Bank, 371 F. Supp. 125 (D. Or. 1974).

221 Applied Digital Data Sys. v. Milgo Elec. Corp., 425 F. Supp. 1145 (S.D.N.Y. 1977); Royal Indus. v. Monogram Indus., [1976-1977 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,863 (C. D. Cal. Nov. 29, 1976); Orbanco, Inc. v. Security Bank, 371 F. Supp. 125 (D. Or. 1974).

222 By requiring a valid business purpose for target management's adoption of certain defensive measures, all of these initial decisions effectively imposed a federal standard of fiduciary duty under § 14(e). The opinions, however, differed on whether a breach of that fiduciary duty constituted a "fraudulent" act, a "deceptive" act, or a "manipulative" act within the meaning of § 14(e). *See* Applied Digital Data Sys. v. Milgo Elec. Corp., 425 F. Supp. 1145, 1158 (S.D.N.Y. 1977) (holding that the breach of fiduciary duty owed to the shareholders was a "fraudulent scheme"); Royal Indus. v. Monogram Indus., [1976-1977 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,863, at 91,136 (C.D. Cal. Nov. 29, 1976) (holding that if a "target makes a defensive acquisition whose . . . primary purpose is to block a tender offer, the [target company] or its man-

suits included a stock option granted to an officer of the target,²²³ the issuance of a large block of stock to a "white knight,"²²⁴ and the acquisition of a corporation to create an antitrust obstacle for the hostile bidder.²²⁵

In 1977, in the same Term *Piper* was decided, the Supreme Court handed down an opinion in *Santa Fe Industries v. Green*²²⁶ that called into question the continued vitality of these initial decisions interpreting section 14(e). In *Santa Fe*, the Supreme Court held that a "short-form," "squeeze-out" merger²²⁷ at an unfair cash price was not a "manipulative or deceptive device" within the meaning of section 10(b) of the Exchange Act because there had been no misrepresentation or nondisclosure regarding the price.²²⁸ The opinion of the Court of Appeals for the Second Circuit in the *Santa Fe* litigation, which was reversed by the Supreme Court, had unequivocally held that a claim could be stated under section 10(b) without any allegation of misrepresentation or nondisclosure and that section 10(b) reached situations in which majority shareholders breached their fiduciary duty to deal fairly with minority shareholders by consummating a securities transaction that lacked a valid business purpose.²²⁹ The Supreme Court maintained that the Second Circuit's interpretation of section 10(b) was unwarranted since it would "federalize the substantial portion of the law of corporations that deals with transactions in securities" without any indication that Congress

agement violates Section 14(e) . . . and their fiduciary duties under Delaware law"); *Orbanco Inc. v. Security Bank*, 371 F. Supp. 125, 128-29 (D. Or. 1974) (holding that the defensive measure was a "manipulative act").

223 *Orbanco, Inc. v. Security Bank*, 371 F. Supp. 125, 128-29 (D. Or. 1974).

224 *Applied Digital Data Sys. v. Milgo Elec. Corp.*, 425 F. Supp. 1145, 1157-58 (S.D.N.Y. 1977).

225 *Royal Indus. v. Monogram Indus.*, [1976-1977 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,863, at 91,136-37 (C.D. Cal. Nov. 29, 1976).

226 430 U.S. 462 (1977). Justice White delivered the opinion in *Santa Fe*, and he was joined by Chief Justice Burger and Justices Stewart, Marshall, Powell, and Rehnquist. Justices Blackmun and Stevens concurred in separate opinions. Justice Brennan dissented.

227 The "short-form" merger in *Santa Fe* was governed by Delaware law, and it is defined by statute as a merger of a 90%-owned subsidiary into its parent corporation. The merger does not require the approval of the shareholders of either corporation, and the minority shareholders of the subsidiary may receive cash for their shares. See DEL. CODE ANN. tit.8, § 253 (1983 & Supp. 1988). A "squeeze-out" merger is any merger in which a controlling corporation uses its control to absorb a controlled corporation. In such a merger, the minority shareholders of the controlled corporation are forced to sell their shares for cash.

228 *Santa Fe*, 430 U.S. at 474-77.

229 *Green v. Santa Fe Indus.*, 533 F.2d 1283, 1289-91 (2d Cir. 1976), *rev'd*, 430 U.S. 462 (1977).

intended such a result.²³⁰ Relying on *Piper*, the Court concluded that "it [was] entirely appropriate to relegate [the minority shareholders] to whatever remedy [was] created by state law."²³¹

After *Santa Fe*, a controversy mounted in the courts of appeals over the intended scope of section 14(e). Specifically, the Courts of Appeals for the Sixth and Second Circuits disagreed on whether section 14(e)'s prohibition against manipulative conduct covered defensive measures frequently employed by targets—"lock-up" and "leg-up" arrangements²³² with a "white knight"—when the arrangements involved no misrepresentation and were fully disclosed.²³³ On the one hand, the Sixth Circuit held that "ma-

230 *Santa Fe*, 430 U.S. at 479.

231 *Id.* at 478 (quoting *Cort v. Ash*, 422 U.S. 66, 84 (1975), and *Piper v. Chris-Craft Indus.*, 430 U.S. 1, 40 (1977)). At the time of the merger in *Santa Fe*, it was assumed that an appraisal remedy was the exclusive remedy available under Delaware law for minority shareholders that were dissatisfied with a "short-form," "cash-out" merger. *See id.* at 465-66; *Stauffer v. Standard Brands Inc.*, 41 Del. Ch. 7, 187 A.2d 78 (1962). Shortly after *Santa Fe*, however, the Supreme Court of Delaware in *Singer v. Magnavox Co.*, 380 A.2d 969 (Del. 1977), held that minority shareholders could sue to enjoin a "short-form" merger if the merger lacked a valid business purpose. In 1985, the Supreme Court of Delaware in *Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983), overruled *Singer* and eliminated the requirement of a valid business purpose; as a result, an appraisal remedy may be the sole remedy in Delaware for minority shareholders who complain that they received an unfair cash price in a "short-form" merger. For an excellent survey of the pre-*Santa Fe* tensions that existed between federal and state law in setting standards of conduct for corporate management, see *Symposium on Federal and State Roles in Establishing Standards of Conduct for Corporate Management*, 31 BUS. LAW. 861 (1976).

Some "squeeze-out" mergers may be subject to rule 13e-3, 17 C.F.R. § 240.13e-3 (1990), if the merger is a "going private" transaction by a public company. *See supra* note 106. The evolution of rule 13e-3 is noteworthy. In 1975, pursuant to its rulemaking power under §§ 10(b) and 13(e), the SEC proposed for comment alternate versions of a rule that would have authorized the SEC to prohibit "going private" transactions that were unfair. *See Notice Rulemaking Proceeding Regarding "Going Private" Transactions*, Exchange Act Release No. 11,231, [1974-1975 Transfer Binder] Fed. Sec. F. Rep. (CCH) ¶ 80,104 (Feb. 6, 1976). One version required that the consideration offered to shareholders in a "going private" transaction be "no lower than the consideration recommended jointly by two qualified independent persons." *Id.* at 85,092. The other version required that a "going private" transaction have a valid business purpose. *Id.* at 85,093. After *Santa Fe*, the SEC backed down from these attempts to regulate the substantive fairness of "going private" transactions, and the final version of rule 13e-3, adopted in 1979, purports to require only "disclosure." Schedule 13E-3, 17 C.F.R. § 240.13e-100 (item 8(a)) (1990), requires a statement whether the company that is "going private" reasonably believes that the transaction is "fair or unfair" to the shareholders.

232 *See infra* text accompanying note 317; *see also infra* note 325 and accompanying text.

233 *Data Probe Acquisition Corp. v. Datatab, Inc.*, 722 F.2d 1 (2d Cir. 1983), *cert. denied*, 465 U.S. 1052 (1984); *Buffalo Forge Co. v. Ogden Corp.*, 717 F.2d 757 (2d Cir.), *cert. denied*, 464 U.S. 1018 (1983); *Mobil Corp. v. Marathon Oil Co.*, 669 F.2d 366 (6th Cir. 1981), *cert. denied*, 455 U.S. 982 (1982). The litigation in all of these cases was instituted by offerors seeking to enjoin the "lock-up" arrangements.

nipulative acts" under section 14(e) did not require misrepresentation or nondisclosure, reasoning that "to find compliance with section 14(e) solely by the full disclosure of manipulative acts as a *fait accompli* would be to read the 'manipulative acts and practices' language completely out of the Williams Act."²³⁴ On the other hand, the Second Circuit concluded that *Santa Fe* was controlling and held, in two separate decisions, that misrepresentation or nondisclosure was a necessary element of manipulative conduct under section 14(e).²³⁵ The Supreme Court denied certiorari in all three cases.²³⁶ Then, when the Court of Appeals for the Third Circuit took the side of the Second Circuit in a case not involving defensive tactics, the Supreme Court granted certiorari to resolve the conflict over the intended meaning of the term "manipulative" in section 14(e).²³⁷ The case reached the Supreme Court as *Schreiber v. Burlington Northern, Inc.*²³⁸

While the controversy was mounting in the courts, legal commentators were also in disagreement. Some argued that §§ 10(b) and 14(e) should not be construed in *pari materia* and that "manipulative acts" under § 14(e) do not require misrepresentation or nondisclosure. Further, they contended that certain fully and fairly disclosed defensive tactics should be proscribed by § 14(e). See, e.g., Junewicz, *The Appropriate Limits of Section 14(e) of the Securities Exchange Act of 1934*, 62 TEX. L. REV. 1171 (1984); Lowenstein, *Section 14(e) of the Williams Act and the Rule 10b-5 Comparisons*, 71 GEO. L.J. 1311 (1983); Weiss, *Defensive Responses to Tender Offers and the Williams Act's Prohibition Against Manipulation*, 35 VAND. L. REV. 1087 (1982); Note, *Target Defensive Tactics as Manipulative Under Section 14(e)*, 84 COL. L. REV. 228 (1984). Others took the opposite viewpoint. See, e.g., Prentice, *Target Board Abuse of Defensive Tactics: Can Federal Law Be Mobilized to Overcome the Business Judgment Rule?*, 8 J. CORP. L. 337 (1983); Note, *Lock-Up Options: Toward a State Law Standard*, 96 HARV. L. REV. 1068 (1983).

234 *Mobil Corp. v. Marathon Oil Co.*, 669 F.2d 366, 377 (6th Cir. 1981), cert. denied, 455 U.S. 982 (1982). The court argued that the challenged arrangements created an artificial price ceiling in the tender offer market for the target's stock, and that they were therefore "manipulative acts" in connection with a tender offer in violation of § 14(e). *Id.* at 375.

235 *Data Probe Acquisition Corp. v. Datatab, Inc.*, 722 F.2d 1, 4 (2d Cir. 1983) (contending that the "gravamen of the claim [was] breach of management's fiduciary duty to shareholders, a matter traditionally committed to state law"), cert. denied, 465 U.S. 1052 (1984); *Buffalo Forge Co. v. Ogden Corp.*, 717 F.2d 757, 760 (2d Cir.), cert. denied, 464 U.S. 1018 (1983).

236 *Data Probe Acquisition Corp. v. Datatab, Inc.*, 464 U.S. 1052 (1984), denying cert. to 722 F.2d 1 (2d Cir. 1983); *Buffalo Forge Co. v. Ogden Corp.*, 464 U.S. 1018, denying cert. to 717 F.2d 757 (2d Cir. 1983); *Mobil Corp. v. Marathon Oil Co.*, 455 U.S. 982 (1982), denying cert. to 699 F.2d 366 (6th Cir. 1981).

237 *Schreiber v. Burlington N., Inc.*, 469 U.S. 815, granting cert. to 731 F.2d 163 (3d Cir. 1984). After the Third Circuit's decision in *Schreiber*, but before the Supreme Court's grant of certiorari, the Court of Appeals for the Eighth Circuit in *Feldbaum v. Avon Prod.*, 741 F.2d 234 (8th Cir. 1984), adopted the view taken by the Second and Third Circuits. The litigation in *Feldbaum* was instituted by a target shareholder seeking damages on account of a "lock-up" option that target management had granted a friendly bidder in order to preclude competition from a third party.

238 472 U.S. 1 (1985). The Court's choice of *Schreiber* as the case to resolve the con-

B. *The Schreiber Case*

1. Denial of Substantive Protections to Target Shareholders

The opinion in *Schreiber*, rendered in 1985, was the Supreme Court's second occasion to interpret the tender offer provisions of the Williams Act. *Schreiber* concerned the successful takeover of the El Paso Company (El Paso) by Burlington Northern, Inc. (Burlington).²³⁹ On December 21, 1982, Burlington launched a hostile cash tender offer for a majority (25,100,000 shares) of El Paso's common stock at \$24 per share. The offer was to expire twenty business days later, on January 19, 1983. Burlington, however, reserved the right to cancel the offer if any of several specified developments occurred.²⁴⁰ El Paso shareholders had the right to withdraw shares tendered until January 12, 1983, and if the offer was oversubscribed, shares tendered by December 30, 1982, would be purchased on a prorated basis.²⁴¹ Burlington's offer provided no price or other protections in the event of a second-step acquisition of the shares not obtained in the tender offer.

On advice from its investment banker, El Paso initially opposed the Burlington offer. El Paso shareholders were informed that management recommended rejection of the offer on the grounds that the \$24 per share offering price was inadequate and that the minority shareholders remaining after the completion of the offer might be adversely affected by a second-step "squeeze-out" merger. Also, El Paso management authorized a variety of defensive measures and searched for better alternatives to the Burlington offer. Nonetheless, the Burlington offer was fully subscribed by the expiration of the proration period. Furthermore, El Paso ultimately realized that \$24 was the highest price obtainable for its shares. Accordingly, El Paso management told Burlington's

troversty over the intended scope of § 14(e) is revealing. The Court obviously preferred a case that did not involve defensive tactics, and by choosing a case that was brought by a target shareholder suing for damages, the Court was able to avoid (as it had in *Piper*) the question whether offerors had standing to sue for injunctive relief under § 14(e).

239 A summary of Burlington's takeover of El Paso is set forth in *id.* at 2-4 and in I A. FLEISCHER, *supra* note 218, at 499-502.

240 The major conditions of El Paso's offer are set forth in *Brill v. Burlington N., Inc.*, 590 F. Supp. 893, 895 n.3 (D. Del. 1984).

241 At the time of Burlington's tender offer, rule 14d-7, 17 C.F.R. § 240.14d-7 (1982), permitted target shareholders to withdraw shares tendered during the first 15 business days of an offer, and the proration period was 10 calendar days. See *supra* notes 83-84 and accompanying text.

representatives that it was interested in discussing an acquisition by Burlington which would be more favorable to El Paso shareholders than Burlington's outstanding offer. Negotiations ensued and an accord was eventually reached. Among other things, Burlington agreed to (1) withdraw the December tender offer pursuant to the "out" clause in its offer and initiate a new tender offer for 21,000,000 shares at \$24 per share, (2) purchase 4,166,667 shares of newly authorized El Paso shares for \$24 per share, and (3) provide that a majority of the continuing El Paso directors and a majority of the non-Burlington El Paso shareholders would have to approve any second-step acquisition of the balance of the El Paso shares.

In accordance with this agreement, Burlington terminated its tender offer on January 10, 1983, and the following day it commenced the new offer. The El Paso shareholders who had tendered to Burlington in the December offer retendered in the January offer. Also, the El Paso directors and other El Paso shareholders who had retained their shares during the December offer tendered in the January offer, and as a result, the January offer was substantially oversubscribed. Burlington eventually purchased, on a prorated basis, 21,000,000 of the over 40,000,000 shares tendered. Consequently, the El Paso shareholders who tendered in both offers had fewer shares accepted for payment in the January offer than would have been accepted in the December offer because the proration pool was larger.

Barbara Schreiber, who was one of these shareholders, brought an action for damages on behalf of herself and other shareholders similarly situated against Burlington, El Paso, and El Paso's board of directors. In the suit, she alleged that Burlington's cancellation of the December tender offer and substitution of the January offer, after negotiations with El Paso, was a manipulative distortion of the market for El Paso shares in violation of the prohibition against "manipulative acts" in section 14(e) of the Williams Act.²⁴² The District Court for the District of Delaware dismissed the suit, holding that the alleged misconduct was not

²⁴² *Schreiber*, 472 U.S. at 4. Schreiber also alleged that Burlington violated § 14(e)'s prohibition of "deceptive acts" in connection with a tender offer by failing in the January offer to disclose that "golden parachutes" had been offered to four members of El Paso's management. *Id.* A "golden parachute" is a special employment agreement between a corporation and its top managers affording financial assurances in the event of a change of corporate ownership.

manipulative because there was no deception.²⁴³ The Court of Appeals for the Third Circuit affirmed the district court's decision. The court reasoned that the Williams Act was primarily a disclosure statute and that Burlington's "arguable breach of contract" was not manipulative conduct because it was fully disclosed.²⁴⁴

The Supreme Court affirmed the Third Circuit's decision, 7-0, in an opinion written by Chief Justice Burger.²⁴⁵ The Court held that "manipulative acts" under section 14(e) require misrepresentation or nondisclosure of the misconduct alleged.²⁴⁶ Accordingly, the Court found that the defendants had not violated section 14(e) because they had made no misrepresentations and their actions were fully disclosed.²⁴⁷ The Court's holding was based on the language, purpose, and legislative history of section 14(e).

At the outset, the Court turned to the language of the phrase "fraudulent, deceptive or manipulative acts or practices" in section 14(e) and opined that since section 10(b) contained the similar phrase "manipulative or deceptive device or contrivance," sections 10(b) and 14(e) should be construed *in pari materia*.²⁴⁸ The Court, therefore, borrowed the definition of the word "manipulative" that it had adopted under section 10(b) in *Ernst & Ernst v. Hochfelder*²⁴⁹ in 1976. Quoting directly from *Hochfelder*, the Court stated that the word "manipulative" was "virtually a term of art when used in connection with the securities markets" and that it connoted "conduct *designed to deceive or defraud* investors by controlling or artificially affecting the price of securities."²⁵⁰ From this definition, the Court somehow deduced that misrepresentation or nondisclosure was a requisite element of all "manipulative acts" under section 14(e). Presumably, the Court reasoned *sub si-*

243 *Schreiber v. Burlington N., Inc.*, 568 F. Supp. 197, 202-03 (D. Del. 1983).

244 *Schreiber v. Burlington N., Inc.*, 731 F.2d 163, 165-66 (3d Cir. 1984).

245 Chief Justice Burger was joined by Justices Brennan, White, Marshall, Blackmun, Rehnquist, and Stevens. Justices Powell and O'Connor took no part in the decision of the case.

246 *Schrieber*, 472 U.S. at 12. The Court also held that the allegedly deceptive "golden parachute" agreements did not cause injury to the plaintiff since these agreements were arranged in connection with the January offer and the plaintiff sought redress only in connection with the December offer. *Id.* at 13.

247 *Id.* at 12-13.

248 *Id.* at 5-8.

249 425 U.S. 185 (1976).

250 *Schreiber*, 472 U.S. at 6 (quoting *Hochfelder*, 425 U.S. at 199) (emphasis added by the *Schreiber* Court).

lento that investors could not be deceived or defrauded by conduct that artificially influenced the price of securities—and thus it could not be reasonably inferred that the conduct was designed to deceive or defraud—unless the conduct involved some form of misrepresentation or unless the conduct was not disclosed.

The Court pointed out that interpreting the term “manipulative” in section 14(e) to signify market or price manipulation comported with the usage of the term at common law and with the traditional dictionary definition of the word “manipulation”—“management with use of unfair, scheming, or underhanded methods.”²⁵¹ The Court also noted that its interpretation was consistent with its holding in *Santa Fe* that the term “manipulative” in section 10(b) did not cover corporate mismanagement unless there was misrepresentation or nondisclosure.²⁵² And finally, the Court rejected the plaintiff’s argument that the use of the disjunctive “or” in section 14(e) indicated that acts could be manipulative even if they were not fraudulent or deceptive. The Court contended that words in a list should be given a similar meaning and that all three types of misconduct listed in section 14(e) involved misrepresentation or nondisclosure.²⁵³

The Court found that its conclusion regarding the meaning of the term “manipulative” as used in section 14(e) was confirmed by the provision’s purpose and legislative history. As in *Piper*, the Court emphasized that the purpose of the Williams Act was to protect target shareholders by requiring disclosure of information.²⁵⁴ The Court maintained that section 14(e) merely supplemented the specific disclosure provisions of the Act and that the substantive safeguards of sections 13(e) and 14(d)—which the Court characterized as narrow—were designed to facilitate disclosure by giving shareholders sufficient time to consider the information that had to be disclosed.²⁵⁵ In the Court’s view, the neutral setting created by the Williams Act was disclosure-oriented also because it served to ensure that each side of a takeover contest would have an equal opportunity to disclose its case.²⁵⁶

251 *Id.* at 7.

252 *Id.* at 7-8 & n.6.

253 *Id.* at 7-8.

254 *Id.* at 8-9.

255 *Id.* at 9-11.

256 *Id.* at 9. In footnote eight of the opinion (*see id.* at 9 n.8), the Court made two observations about § 13(e) to buttress its conclusion that the Williams Act and § 14(e) were concerned with disclosure. The two observations, however, were somewhat inconsistent, and they did not unequivocally support the proposition advanced. First, the

Then, after observing that the legislative history regarding section 14(e) was sparse, the Court contended that there was no evidence in the legislative documents suggesting that section 14(e) was directed at any purpose other than disclosure or that the prohibition in section 14(e) against manipulative conduct was meant to encompass fully disclosed "artificial" or "unfair" conduct.²⁵⁷

2. An Analysis of *Schreiber*

The opinion in *Schreiber* did double duty for the Court. It legitimized under federal law not only the specific conduct of the offeror and the target in the *Schreiber* litigation, but also a variety of defensive tactics employed by targets in other takeovers.²⁵⁸ The Court was able to decide two cases in one by framing the issue broadly—whether misrepresentation or nondisclosure is an essential ingredient of section 14(e) manipulative conduct. Furthermore, the Court's affirmative holding on this issue made the disposition of both cases relatively straightforward since the defendants' activities were, and defensive tactics usually are, fully and fairly disclosed. That *Schreiber* was meant to extend to defen-

Court attempted to demonstrate that the Williams Act was disclosure-oriented by showing that § 13(e) was a disclosure provision. The Court indicated that Congress "impose[d] specific disclosure duties" in § 13(e) to address the concern that issuer repurchases could be used to distort the market for corporate control. But § 13(e) does not impose *any* duties. It gives the SEC the power to adopt rules that define—and prescribe means reasonably designed to prevent—fraudulent, deceptive, or manipulative practices in connection with a company's purchases of its own securities. Then, § 13(e) indicates that these rules may require that the company make appropriate disclosures to its shareholders. See *supra* note 101. There is no indication in § 13(e), however, that the SEC's power is limited to adopting disclosure requirements. See *supra* note 109 and accompanying text. Second, the Court purported to underscore that § 14(e) was devoid of substantive content by pointing out that it would have been unnecessary for Congress to grant the SEC the power to *regulate* issuer repurchases if

§ 14(e) was meant to *forbid* "artificial" or "unfair" purchases by a company of its own stock during the course of a third-party tender offer. But § 13(e) governs all issuer repurchases, whether or not a third-party offer is outstanding, whereas § 14(e) is addressed only to the tender offer context. Therefore, the scope of § 13(e) is different from that of § 14(e). Furthermore, if § 13(e) gives the SEC "broad regulatory power" to regulate the substantive aspects of issuer repurchases, as the footnote suggests that it does, § 14(e) should also have some substantive significance since §§ 13(e) and 14(e) contain virtually identical language. See Fiffis, *Of Lollipops and Law—A Proposal for a National Policy Concerning Tender Offer Defenses*, 19 U.C. DAVIS L. REV. 303, 324-25 (1986).

²⁵⁷ *Schreiber*, 472 U.S. at 11-12. The Court believed that judges should not impose their own notions of "artificiality" or "fairness." *Id.* at 9 n.8, 12.

²⁵⁸ El Paso's agreement to sell 4,166,667 shares to Burlington, see *id.* at 3, is similar to a "leg-up" agreement. See Bloomenthal, *RICO, Pari Delicto, Deception, and the Supreme Court*, 7 Sec. & Fed. Corp. L. Rep. (Clark Boardman) 49, 54 (July-Aug. 1985); *infra* note 325 and accompanying text.

sive tactics, however, could have been easily missed.²⁵⁹ Only a footnote in the opinion explained that the Court had granted certiorari to resolve the appellate-court controversy over defensive tactics.²⁶⁰ Moreover, the conduct in *Schreiber*—a bidder's withdrawal of a hostile offer followed by a friendly offer after a rapprochement between the bidder and target—did not squarely pose the same legal issues that arise when a target adopts defensive measures to thwart a hostile offer. In this regard, there is some question whether *Schreiber* was even the appropriate case to resolve the controversy. An opinion that placed a number of defensive maneuvers outside the reach of federal law should have been rendered only after briefs and arguments directly on point were presented by parties that had a genuine stake in the outcome.²⁶¹

If the Court in *Schreiber* had not set out to resolve the controversy over defensive tactics, the opinion could have reached the same result without grappling with the question whether misrepresentation or nondisclosure is a requisite element of manipulative conduct under section 14(e). Foremost, the Court could have held that the defendants' activities were not manipulative because they were not "artificial."²⁶² According to the Court, for conduct to be manipulative, the price of securities must be influenced by artificial means,²⁶³ that is, by means unrelated to the natural forces of supply and demand.²⁶⁴ The Court could have easily ruled *sua sponte* that while the defendants' conduct may have affected the price of El Paso stock, it did not do so artificially. There was no evidence in the record indicating that the defendants' activities distorted the price of El Paso stock.²⁶⁵ Moreover, to say that there was a distortion would be tantamount to characterizing all withdrawals and renegotiations of tender offers as artificial practices.

In addition, if the Court had deigned to evaluate the substantive fairness of the defendants' activities and had not backed down from its observation that one of the dictionary definitions

259 See Bloomenthal, *supra* note 258, at 53.

260 *Schreiber*, 472 U.S. at 5 n.3.

261 See Bloomenthal, *supra* note 258, at 53-54; *infra* note 338.

262 See *supra* note 257 and accompanying text.

263 See *supra* text accompanying note 250.

264 *Mobil Corp. v. Marathon Oil Co.*, 669 F.2d 366, 374 (6th Cir. 1981), *cert. denied*, 455 U.S. 982 (1982).

265 See Bloomenthal, *supra* note 258, at 54.

of the word "manipulation" was "management with use of unfair methods," the Court could have concluded that the defendants' activities were not manipulative because they were not "unfair." Throughout the transactions at issue, the directors of El Paso acted fairly and in the best interests of the *entire* body of El Paso shareholders. At first, the directors opposed the Burlington offer and "shopped" the company to obtain a better offer. Then, after these efforts were unsuccessful, the board negotiated an improved offer with Burlington. Although this offer benefitted the shareholder-directors (because it enabled them to tender their shares) and harmed the shareholders who had tendered in the first offer (because their proration position was lost), the directors' actions in negotiating this offer served an overriding interest of the corporation and protected all shareholders as a group. First, the directors were able to obtain procedural "back-end" protections that eliminated the offensive aspects of Burlington's initial offer. Second, by insisting that the substituted offer be structured as a new offer, the directors afforded the shareholders who had not tendered in the first offer (presumably because of the board's opposition) an opportunity to tender into the improved offer.²⁶⁶ Burlington also treated the El Paso shareholders fairly. The shareholders who had tendered in the first offer had no vested right to have their shares accepted for payment since Burlington's offer clearly stipulated that it could be revoked if certain bona fide conditions occurred. Such a stipulation is common in tender offers and is not prohibited by federal or state law. Because several of the conditions contained in Burlington's offer did occur, Burlington's termination of the offer was not unfair to the shareholders who had already deposited their shares.²⁶⁷

The true vice of *Schreiber*, however, was not that the Court took on the controversy over defensive tender offer tactics unnecessarily, but that it resolved the controversy incorrectly by misinterpreting section 14(e). The Court was on firm ground in ruling that market manipulation is barred by section 14(e) and that market manipulation requires some form of misrepresentation or

²⁶⁶ See *Gilbert v. El Paso Co.*, 575 A.2d 1131, 1148 (Del. 1990) (holding that the El Paso directors did not breach their fiduciary duty of care and loyalty owed to El Paso and its shareholders under Delaware law).

²⁶⁷ See *Gilbert v. El Paso Co.*, 490 A.2d 1050 (Del. Ch. 1984) (holding that Burlington's revocation of the December offer did not constitute a breach of a contractual or fiduciary obligation owed to the El Paso shareholders under state law), *aff'd*, 575 A.2d 1131 (Del. 1990); *infra* text accompanying notes 354-58.

nondisclosure. But, the Court's conclusion that misrepresentation or nondisclosure is a necessary element of all manipulative conduct proscribed by section 14(e) was erroneous. Congress intended section 14(e) to prohibit another species of manipulation—one that is not grounded in misrepresentation or a failure to disclose. Although this prohibition does not cover the defendants' activities in *Schreiber*, it does encompass many of the defensive tactics employed by targets.

(a) *The Prohibition in Section 14(e) Against Market Manipulation.*—Before the passage of the Exchange Act in 1934, conduct that artificially raised or depressed the price of securities in the trading markets was considered unlawful at common law when the purpose of the conduct was to mislead investors as to the true value of the securities.²⁶⁸ This conduct, called market or price manipulation,²⁶⁹ generally consisted of the dissemination of fictitious reports about a company's earnings²⁷⁰ or artificial acts of stimulative trading in a company's securities.²⁷¹ For example, wash sales (transactions in which the market operator bought and then sold the same stock at the same price) and matched orders (transactions in which the operator entered a buy order knowing that a confederate was simultaneously entering a sell order for the same stock at the same price) were usually condemned as manipulative under the common law.²⁷² These

268 See generally Berle, *Liability for Stock Market Manipulation*, 31 COLUM. L. REV. 264 (1931). Before the Exchange Act, the major market manipulators were groups (pools) of speculators known as either "bears" or "bulls." Bears sold stock that they had borrowed and then drove down the price by covertly selling large quantities of the stock (a "bear raid") so that they could cover their short position at the artificially depressed price. Bulls, on the other hand, made secret purchases of a single stock so as to raise its price and then sold the stock to the public at a profit. Bulls also made profits by obtaining control over a large part of the supply of stock (a "corner") that bears needed in order to cover their short position. By doing this, bulls were able to force bears to buy the stock from them at an inflated price. See Moore & Wiseman, *Market Manipulation and the Exchange Act*, 2 U. CHI. L. REV. 46, 51 n.27 (1934); Poser, *Stock Market Manipulation and Corporate Control Transactions*, 40 U. MIAMI L. REV. 671, 692 (1986); Comment, *Market Manipulation and the Securities Exchange Act*, 46 YALE L.J. 624, 626-28 (1937).

269 The word "manipulation" derives from the Latin word for "hand," *manus*, and has been aptly described as "the laying of hands on the scales." L. LOSS, *supra* note 3, at 845.

270 See *Harris v. United States*, 48 F.2d 771 (9th Cir. 1931); see also Note, *Regulation of Stock Market Manipulation*, 56 YALE L.J. 509, 512 (1947).

271 See *United States v. Brown*, 5 F. Supp. 81 (S.D.N.Y. 1933), *aff'd*, 79 F.2d 321 (2d Cir.), *cert. denied*, 296 U.S. 650 (1935); Comment, *supra* note 268, at 626-28.

272 See *Harris v. United States*, 48 F.2d 771 (9th Cir. 1931); Comment, *supra* note 268, at 627; Note, *supra* note 270, at 513. A sale and an immediate repurchase of a

practices misinformed the public by falsifying an appearance of market activity and by creating a price not reflective of supply and demand.

The legislative history of the Exchange Act indicates that Congress intended to incorporate the common-law concept of manipulation into the federal legislation and expand upon it so as to beef up the attack against market manipulators.²⁷³ This objective was accomplished, in part, by section 9,²⁷⁴ which is entitled "Prohibition Against Manipulation of Security Prices." The text of section 9 never uses the words "manipulation" or "manipulative"²⁷⁵ but outlaws a series of deceptive practices, most of which constituted manipulation at common law.²⁷⁶ In addition to wash sales and matched orders,²⁷⁷ these practices include manipulation of the market by rigged prices,²⁷⁸ rumors,²⁷⁹ false or misleading statements,²⁸⁰ paid touts,²⁸¹ and stabilization.²⁸²

security for the purpose of obtaining a higher cost basis in the security for tax purposes has never been considered an illegal manipulative practice. Likewise, a broker's crossing of buy and sell orders at the same price has never been regarded as manipulative per se. See L. LOSS, *supra* note 3, at 851 n.22.

273 Berle, *supra* note 268, at 393 (indicating that the Exchange Act created remedies and compliance mechanisms for common law manipulation); Poser, *supra* note 268, at 690 (indicating that "one of the purposes of the Exchange Act was to make illegal certain stock-market practices that were then regarded as manipulative but were not illegal [under the common law]").

274 15 U.S.C. § 78i (1988).

275 When referring to § 9, the House report, however, uses the phrase "manipulative practices". See H.R. REP. NO. 1383, 73d Cong., 2d Sess. 10-11 (1934). Also, § 2 of the Exchange Act, 15 U.S.C. § 78b (1988), entitled "Necessity for Regulation as Provided in This Title," speaks in terms of the "manipulation . . . of security prices."

276 See Poser, *supra* note 268, at 690-705. Section 9(e), 15 U.S.C. § 78i(e) (1988), provides an express private remedy for investors injured by the conduct forbidden by § 9.

277 15 U.S.C. § 78i(a)(1) (1988). Section 9(a)(1) provides that wash sales or matched orders are unlawful only if their purpose is to create "a false or misleading appearance of active trading . . . or a false or misleading appearance with respect to the market for any . . . security."

278 *Id.* § 78i(a)(2). Section 9(a)(2) makes it unlawful "[t]o effect . . . a series of transactions . . . creating actual or apparent active trading in [a] security or raising or depressing the price of [a] security, for the purpose of inducing the purchase or sale of [the] security by others."

279 *Id.* § 78i(a)(3). Section 9(a)(3) makes it unlawful "to induce the purchase or sale of [a] security . . . by the circulation or dissemination in the ordinary course of business of information to the effect that the price of [the] security will or is likely to rise because of market operations conducted for the purpose of raising or depressing the price of [the] security."

280 *Id.* § 78i(a)(4). The false or misleading statement must be made for "the purpose of inducing the purchase or sale of [a] security."

281 *Id.* § 78i(a)(5). Section 9(a)(5) makes it unlawful to engage in the acts proscribed by § 9(a)(3) (see *supra* note 277) for a consideration.

282 *Id.* § 78i(a)(6). Section 9(a)(6) makes it unlawful "to effect . . . a series of

Since section 9 applies only when the proscribed activities occur with respect to securities listed on a national securities exchange,²⁸³ Congress rounded out its attack on market manipulation in sections 10(b),²⁸⁴ 15(c)(1), and 15(c)(2).²⁸⁵ Section 10(b) makes it unlawful for *any person* to use, in connection with the purchase or sale of *any security*, any "manipulative or deceptive device or contrivance" in contravention of rules that the SEC may adopt.²⁸⁶ Sections 15(c)(1) and 15(c)(2) prohibit "manipulative," "deceptive," and "fraudulent," conduct by broker-dealers in the over-the-counter market.²⁸⁷ Although it has been generally ac-

transactions for the purchase and/or sale of [a] security . . . for the purpose of pegging, fixing, or stabilizing the price of such security" in contravention of rules that the SEC may adopt. Stabilization, which is the generic term, involves holding the price of a security at a constant or predetermined level by purchasing and/or selling the security. Stabilization has been described as "a relatively benign form of manipulation." L. LOSS, *supra* note 3, at 849. The SEC has adopted several rules governing stabilization during a public distribution—rules 10b-6, 10b-7, and 10b-8, 17 C.F.R. § 240.10b-6 to -8 (1990). Rule 10b-6 prohibits a person connected with a public distribution from purchasing and/or selling the security which is the subject of the distribution unless the transaction is made in compliance with rules 10b-7 and 10b-8. These rules were adopted primarily under § 10(b) because § 9(a) is limited to registered securities. *See* L. LOSS, *supra* note 3, at 862 n.82. The SEC has also addressed stabilization in the tender offer context. *See* 2 T. HAZEN, *supra* note 56, § 12.1, at 5. Rule 10b-13, 17 C.F.R. § 240.10b-13 (1990), prohibits a person who makes a tender offer for an equity security from buying such security outside the offer. In adopting rule 10b-13, the SEC stated that buying "alongside the offer" was a manipulative practice because it 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." Adoption of Rule 10b-13, Exchange Act Release No. 8712, [1969-1970 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 77,745, at 83,708 (Oct. 8, 1969). Rule 10b-13 was not adopted under § 9(a)(6) but under §§ 10(b), 13(e), and 14(e). *Id.* at 83,709. Last, the SEC has adopted rule 10b-18, 17 C.F.R. § 240.10b-18 (1990), which is designed, in part, to provide a safe harbor for an issuer seeking to stabilize the price of its common stock by repurchase programs. Rule 10b-18 does not cover repurchases subject to rules 13e-1 or 13e-4. *Id.* § 240.10b-18(a)(3)(iv),(v). Rule 10b-18 was adopted under §§ 9(a)(6), 10(b), and 13(e). Adoption of Safe Harbor for Purchases by an Issuer, Exchange Act Release No. 19,244, [1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,276, at 85,486 (Nov. 17, 1982).

283 15 U.S.C. § 78i(a) (1988).

284 *Id.* § 78j(b).

285 Section 15(c)(1) was added to the Exchange Act in 1936. Act of May 27, 1936, ch. 462, sec. 3, § 15(c), 49 Stat. 1375, 1378 (codified as amended at 15 U.S.C. § 78o(c)(1) (1988)). Section 15(c)(2) was added in 1938. Maloney Act, ch. 677, sec. 2, § 15(c)(2), 52 Stat. 1070, 1075 (1938) (codified as amended at 15 U.S.C. § 78o(c)(2) (1988)).

286 15 U.S.C. § 78j(b) (1988).

287 *Id.* § 78o(c)(1)-(2). Section 15(c)(1) makes it unlawful for any broker-dealer "to effect any transaction, or to induce or attempt to induce the purchase or sale of, any security . . . by means of any manipulative, deceptive, or other fraudulent device or contrivance" and gives the SEC rulemaking power to "define such devices and contrivances as are manipulative, deceptive, or otherwise fraudulent." Section 15(c)(2) makes it unlaw-

cepted that sections 10(b) and 15(c) were meant to cover the market manipulation outlawed by section 9,²⁸⁸ neither section 10(b) nor section 15(c) delineates the intended relationship among the words "manipulative," "deceptive," and "fraudulent" or the type of conduct that each word connotes. Thus, when Congress borrowed the same three words for section 14(e) of the Williams Act in 1968, it chose words that did not have an exact meaning.²⁸⁹

Schreiber concluded that Congress used the word "manipulative" in section 14(e) in its technical sense to refer to market manipulation.²⁹⁰ The legislative history of the Williams Act does not explicitly confirm this conclusion, but the legislative documents do reflect congressional solicitude about the manipulation of prices during the course of a tender offer. Senator Williams himself declared: "Efforts are often made to influence the price of the securities involved."²⁹¹ And Senator Williams was right. In one takeover battle, for example, a target's defensive merger partner made open-market purchases and secret off-market sales of the target's stock in order to make the market price of the target's stock exceed the tender offer price and deter target shareholders from tendering their shares to the hostile offeror.²⁹² It

ful for any broker-dealer "to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security . . . in connection with which such broker or dealer engages in any fraudulent, deceptive, or manipulative act or practice, or makes any fictitious quotation" and gives the SEC rulemaking power to "define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative and such quotations as are fictitious."

288 See *SEC v. Resch-Cassin & Co.*, 362 F. Supp. 964, 975 (S.D.N.Y. 1973); L. LOSS, *supra* note 3, at 850, 857-59. The House report that accompanied § 10(b) indicated that the control of manipulative practices would ensure "markets where prices may be established by the free and honest balancing of investment demand and supply." H.R. REP. NO. 1383, *supra* note 275, at 10. Also, the Senate report that accompanied an earlier version of § 10(b) referred to the prohibition of "devices . . . employed for the purpose of artificially raising or depressing security prices." S. REP. NO. 792, 73d Cong., 2d Sess. 7 (1934).

289 Cf. L. LOSS, *supra* note 3, at 860 n.75.

290 See *supra* text accompanying note 250.

291 116 CONG. REC. 3024 (1970) (statement of Sen. Williams). Senator Williams made this statement during Congress' consideration of the 1970 amendments to the Williams Act.

292 See *Crane Co. v. Westinghouse Air Brake Co.*, 419 F.2d 787 (2d Cir. 1969), *cert. denied*, 400 U.S. 822 (1970). The takeover battle in *Crane* occurred prior to the adoption of the Williams Act. *Id.* at 790-802. The court held that the defendant's conduct violated §§ 9(a)(2) and 10(b). With respect to its holding under § 10(b), the court found that the defendant was an "insider" of the target company and that the failure to disclose its manipulation was a deceptive act in violation of § 10(b). *Id.* 793-99. When an exchange tender offer is involved, efforts are often made to increase the price of the offeror's

seems fair to assume, therefore, that Congress intended the word "manipulative" to take on at least its technical meaning in section 14(e). Hence, it is hard to cavil with *Schreiber's* observation that section 14(e) bars market manipulation.

It is also difficult to quibble with *Schreiber's* conclusion that market manipulation requires misrepresentation or nondisclosure.²⁹³ As discussed above, market manipulation at common law and under the Exchange Act has always involved deception, by either false words or fictitious acts.²⁹⁴ The nondisclosure component of the Court's formulation brings manipulation by fictitious deeds within conventional theories of fraud by requiring proof that the deeds have not been disclosed.²⁹⁵ This aspect of the Court's concept of market manipulation was not novel. Prior to *Schreiber*, the SEC and the courts had frequently held that when manipulation occurs as a result of stimulative trading, a failure to disclose that the market price has been artificially inflated by the trading is deceptive.²⁹⁶ Of course, requiring proof of nondisclosure in this situation is not particularly consequential since, as the Court in *Schreiber* recognized, "nondisclosure is usually essential to the success of a manipulative scheme."²⁹⁷

stock in order to encourage target shareholders to tender. *See, e.g., Davis v. Pennzoil Co.*, 437 Pa. 194, 207-08, 264 A.2d 597, 603 (1970).

293 *See supra* text accompanying note 246.

294 *See supra* text accompanying notes 268-70; *see also Schreiber*, 472 U.S. at 7 n.4. The object of all market manipulation is to misrepresent the price of a security to the public, and the means used to accomplish this object is misrepresentation (false words) or nondisclosure of fictitious acts. The *Schreiber* Court's holding that manipulation under § 14(e) requires misrepresentation or nondisclosure refers to the *means* used and not the *object* sought.

295 The Court's formulation would seem to govern all the general anti-manipulation provisions of the Exchange Act—§§ 10(b), 14(e), and 15(c)—but not § 9, which is specific as to the elements that must be proven in order to establish a violation. For example, a party suing under § 9(a)(2) should not have to prove nondisclosure of the manipulation; proof that a false market appearance was created by trading should suffice. *See L. LOSS, supra* note 3, at 530 n.137.

296 *See, e.g., In re Barrett & Co.*, 9 S.E.C. 319, 328-39 (1941); *SEC v. Management Dynamics*, 515 F.2d 801, 810 (2d Cir. 1975); *see also L. LOSS, supra* note 3, at 858 & n.67 (citing cases).

297 *Schreiber*, 472 U.S. at 7 (quoting *Santa Fe Indus. v. Green*, 430 U.S. 462, 477 (1977), citing 3 L. LOSS, *supra* note 188, at 1565). In his treatise, Professor Loss actually stated that "non-disclosure of a manipulation is usually, if not invariably, essential to its success." L. LOSS, *supra* note 3, at 1565 (emphasis added).

Since Congress' ban on market manipulation in §§ 10(b) and 14(e) is universal and since a manipulative scheme that is fully and fairly disclosed should not be capable of manipulating the price of securities, it would seem to be a matter of semantics whether one says that liability for market manipulation under §§ 10(b) or 14(e) is predicated on a failure to disclose the manipulation or on the manipulative activity itself. The *Schreiber*

(b) *The Prohibition in Section 14(e) Against the Manipulation of Target Shareholders.*—Despite its accurate formulation of market manipulation, the *Schreiber* Court was wrong in concluding that misrepresentation or nondisclosure is an essential ingredient of all manipulative conduct barred by section 14(e).²⁹⁸ There is material evidence in the legislative record—which the *Schreiber* Court failed to take into account—indicating that section 14(e) was intended to embrace another form of manipulation. This type of manipulation, unlike market manipulation, does not require misrepresentation or nondisclosure. In testimony regarding the role that the SEC should play in the regulation of tender offers, the Chairman of the SEC stated:

[T]here is involved a form of industrial warfare in which the stakes are high, and two or more groups are attempting to *manipulate the public security holder* to their own advantage

. . . .
 . . . [The SEC's] responsibility should be limited to requiring appropriate disclosures, to guarding against *deceptive and unfair devices designed to coerce or prevent action*, and it should be provided with adequate tools to deal effectively with the various techniques that have been developed, and are continuing to be devised to seek or prevent takeover bids
 Finally, authority must be accorded to deal with the violations

Court preferred the former rhetoric and, as a consequence, opined that §§. 10(b) and 14(e) impose on every market manipulator an absolute duty to disclose the manipulation. Some legal commentators, however, have argued (both before and after *Schreiber*) that the use of the word "usually" in *Santa Fe* is significant and that not all manipulative schemes require nondisclosure. See, e.g., Fiffis, *supra* note 256, at 315-16 (arguing that "bear raids" and "corners" (see *supra* note 268) do not require deceit); Junewicz, *supra* note 233, at 1184-85 (arguing that three types of manipulation proscribed by § 9—rumors, paid touts, and stabilization—do not require nondisclosure). Although it is curious that the Court in *Santa Fe* used the word "usually" rather than "always," a scheme to manipulate security prices will not work if it is publicly disclosed. And the examples provided by the commentators cited above are not exceptions to this rule. "Bear raids" and "corners" are forms of price rigging that will not be successful if they are publicly disclosed. Likewise, when market operators or paid touts spread rumors about certain market operations in a security, the price of the security will not be affected if the motives or consequences of the manipulator's actions are fully disclosed. Finally, stabilizing purchases will not be successful in pegging the price of a security if the public is aware of the nature of the purchases. Stabilizing purchases are disclosed on the ticker tape, but they are not distinguished from nonstabilizing purchases. See L. LOSS, *supra* note 3, at 860.

298 *But see* Poser, *supra* note 268 (concluding that the *Schreiber* Court was correct in holding that misrepresentation or nondisclosure is a necessary element of all forms of manipulative conduct forbidden by § 14(e)).

of these precepts—all designed to give investors the *fairest possible opportunity to make his own investment decisions*.²⁹⁹

Although there are few certitudes, it is reasonable to infer from these unrefuted statements that Congress intended the “manipulative acts” proscribed by section 14(e) to include unfair, nondeceptive conduct designed to coerce or prevent the investment decisions of target shareholders.³⁰⁰

This interpretation of the word “manipulative” is consistent with the word’s meaning in everyday speech and with the traditional dictionary definition referenced by the Court.³⁰¹ In common parlance, we speak of the manipulation of persons,³⁰² and especially when they are powerless to prevent it, persons can be manipulated without being deceived.³⁰³ And while the manipulation of persons was not deemed wrongful at common law, the federal securities laws were not intended to be coextensive with common law doctrines; rather they were enacted to rectify deficiencies in the common law by proscribing a wider range of conduct.³⁰⁴ Furthermore, construing the word “manipulative” in section 14(e) in accordance with its vernacular usage to signify the manipulation of target shareholders does not in any way subvert the word’s use in section 14(e) as a technical term to connote market manipulation. Congress was mindful that two meanings existed, and it simply intended the word “manipulative” to take on both meanings in section 14(e).³⁰⁵

299 *House Hearings, supra* note 56, at 11 (statement of Manuel F. Cohen, Chairman, SEC).

300 Although these statements were made by the Chairman of the SEC, it seems appropriate to assume that they express Congress’ intention since at no point subsequent to these hearings did Congress question the precepts that the statements embody. Furthermore, even though the statements do not refer to specific sections of the bills under consideration, it seems safe to conclude that the sections of the bills directed at “requiring appropriate disclosures” became § 14(d) of the Act and that the sections of the bills directed at preventing “deceptive and unfair practices” became § 14(e). *See Data Probe Acquisition Corp. v. Datatab, Inc.*, 568 F. Supp. 1538, 1545-51 (S.D.N.Y.) (contending that Congress intended § 14(e)’s prohibition against “manipulative acts” to extend to practices that fall short of classic market manipulation if they unduly interfere with the tender offer process), *rev’d*, 722 F.2d 1 (2d Cir. 1983), *cert. denied*, 465 U.S. 1052 (1984).

301 *See supra* text accompanying note 251.

302 Section 14(e) outlaws deceit, fraud, and manipulation, and since it is persons who are deceived and defrauded, it seems eminently reasonable to conclude that it is also persons who are manipulated.

303 *See Fiftis, supra* note 256, at 314-15.

304 *See Herman & MacLean v. Huddleston*, 459 U.S. 375, 389 (1983).

305 Of course, it is plausible that Congress used the word “manipulative” in § 14(e) only in its vernacular sense, realizing that market manipulation would be proscribed as a

Interpreting the word "manipulative" in section 14(e) in this manner comports with the intended scope of the word "manipulative" in section 10(b)'s prohibition of conduct deemed by the SEC to be a "manipulative or deceptive device or contrivance." In 1934, a spokesman for the drafters of the provision that was to become section 10(b) indicated that the provision could be paraphrased as "[t]hou shalt not devise any other *cunning* devices." He then explained that the provision was "a catch-all clause to prevent manipulative devices."³⁰⁶ It is difficult to believe that a legislative spokesman would use the words "cunning" and "manipulative" synonymously and refer to the provision as a catchall clause if market manipulation was the only manipulative device that Congress intended the provision to address. As a catchall clause of a statute that sought, as one of its two stated purposes, "to prevent inequitable and unfair practices," section 10(b) surely contemplated the formulation of some standard of substantive fairness for transactions in securities.³⁰⁷

The conclusion that "manipulative acts" under section 14(e) include unfair practices designed to coerce or prevent the decisionmaking of target shareholders is fortified by a consideration of the type of substantive conduct that Congress chose to regulate in section 14(d). As discussed in Part I of the Article, the substantive regulatory scheme of section 14(d), as it existed in 1968, required offerors to allow target shareholders who had tendered to withdraw their shares during the first seven calendar days of the offer. Section 14(d) also required offerors to purchase pro rata any shares deposited during the first ten calendar days of the offer.³⁰⁸ Congress prescribed these specific substantive requirements to curb two unfair practices that bidders had employed prior to the adoption of the Williams Act: launching offers of unduly short duration and accepting shares on a first-come, first-served basis.³⁰⁹ Congress maintained that these two practic-

§ 14(e) "deceptive" act.

306 *Stock Exchange Regulation: Hearings on H.R. 7852 and H.R. 8720 Before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 2d Sess. 115 (1934) (statement of Thomas G. Corcoran). The Supreme Court referred to this legislative history in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 202-03 (1976).

307 See Securities Exchange Act, ch. 404, 48 Stat. 881 (1934) (indicating that the statute is "[a]n Act [t]o provide for the regulation of securities exchanges and of over-the-counter markets operating in interstate and foreign commerce and through the mails, to prevent inequitable and unfair practices on such exchanges and markets and for other purposes").

308 See *supra* text accompanying notes 83-84.

309 See *supra* note 84; cf. *supra* text preceding note 96. In 1968, § 14(d)(5) (statutory

es warranted regulation because they pressured or coerced target shareholders to tender their shares.³¹⁰ The term "manipulative" naturally comes to mind when describing these practices, and no doubt Congress viewed these practices as examples of manipulative conduct.

Section 14(d)'s specific substantive regulation of unfair, coercive practices was necessarily limited to practices that Congress understood in 1968. Congress realized, however, that in the future bidders or targets might devise other unfair practices or targets to distort or abort the investment decisions of target shareholders and that some legislative action was necessary to prevent and guard against these unborn practices.³¹¹ Since section 14(e) supplements section 14(d),³¹² it seems entirely appropriate to assume that both the prohibition against "manipulative acts" in section 14(e) and the 1970 amendment to section 14(e) giving the SEC rulemaking power to define and prescribe means reasonably designed to prevent "manipulative acts"³¹³ were directed primarily at this concern.

Finally, the objectives of the Williams Act confirm this Article's conclusion regarding the substantive coverage of section 14(e). Indeed, the two objectives of the Act³¹⁴ demand that the antimanipulation language in section 14(e) be construed to reach unfair conduct that coerces or prevents the investment decisions of target shareholders. In the first place, Congress' goal of protecting target shareholders by ensuring that they receive full and

withdrawal rights) implicitly created a minimum offering period of seven calendar days for any-or-all offers, and § 14(d)(6) (statutory pro rata rights), by requiring a bidder to purchase pro rata any shares deposited during the first 10 calendar days in partial offers, effectively established a minimum offering period of 10 calendar days for partial offers. See Notice of Proposed Rule 13e-4, Exchange Act Release No. 14,234, [1977-1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 81,380, at 88,785 (Dec. 7, 1977); E. ARANOW & H. EINHORN, *supra* note 3, at 50-52; Note, *SEC Tender Offer Timing Rules: Upsetting a Congressionally Selected Balance*, 68 CORNELL L. REV. 914, 915 (1983). In 1979, the SEC chose to attack directly the problem created by offers of short duration by adopting rule 14e-1, 17 C.F.R. § 240.14e-1 (1990), which requires all offers to remain open for at least 20 business days. See *supra* text preceding note 96.

310 Section 14(d)(7), which ensures that all tendering shareholders receive any increase in price, is not aimed at curbing coercive practices of bidders; rather, it is simply a provision designed to achieve equal treatment of target shareholders.

311 See *supra* text preceding note 299 (statement of Manuel F. Cohen, Chairman, SEC).

312 The *Schreiber* Court stated that § 14(e) "supplements the more precise disclosure provisions found elsewhere in the Williams Act." *Schreiber*, 472 U.S. at 10-11.

313 See *supra* note 95 and accompanying text.

314 See *supra* text accompanying note 53.

true information is substantially impaired if section 14(e) does not ban the use of unfair practices that deny target shareholders the opportunity to act freely, or the opportunity to act at all, on the information that is disclosed.³¹⁵ And second, the neutral regulatory balance that Congress so assiduously sought to attain in crafting the Act is effectively dismantled if section 14(e) is endowed with no substantive content. As suggested above, section 14(d) is a lopsided provision as far as the regulation of substantive conduct is concerned. It imposes specific requirements on bidders to ensure that target shareholders are not unfairly pressured into accepting offers, without imposing comparable strictures on the conduct of target companies in defense.³¹⁶ Therefore, if section 14(e) does not rectify this imbalance by guaranteeing the substantive fairness of the conduct of target management, the scales are markedly tipped in favor of targets.

In the years after the passage of the Williams Act, target companies did in fact devise defensive tender offer tactics that Congress had not envisioned in 1968. Many of these tactics are quintessential "manipulative acts" under section 14(e) because they unfairly deprive target shareholders of an opportunity to make a choice. For example, "lock-up" options and agreements that give a "white knight" the right to buy the target's unissued or treasury shares or its "crown jewels"³¹⁷ are manipulative per se since their purpose is to deter competition from a hostile bidder and coerce target shareholders to tender into an offer made by the "white knight."³¹⁸ Likewise, other measures taken by a target's board of directors that are designed to forestall a hostile offer—such as "poison pills,"³¹⁹ "shark repellent" amendments to a

315 See Karjala, *supra* note 180, at 1501 (arguing that "it makes little sense for detailed information to be delivered if the shareholders are denied the opportunity to act upon it"); Levine, Lykos & Chafetz, *Application of the Federal Securities Laws to Defensive Tactics in Control Contests*, in TENDER OFFERS: DEVELOPMENTS AND COMMENTARIES 193, 205 (M. Steinberg ed. 1985) (arguing that "there is no value in requiring that information be provided shareholders if the opportunity to use such information to make an investment decision is precluded").

316 See *supra* text accompanying notes 308-09.

317 "Crown jewels" are the target's most valuable assets.

318 "Lock-up" options may be granted to a "white knight" to preclude a hostile offer from ever being launched or to defeat a hostile offer that is already outstanding.

319 In general, the term "poison pill" refers to a shareholder rights plan under which an actual or putative target company distributes "rights" to its shareholders. A rights plan usually contains both "flip-in" and "flip-over" provisions. The "flip-in" provision entitles the target shareholders to purchase common stock of the target (at a price which is usually one-half of the market price) if any person acquires target stock in excess of a certain percentage of the outstanding stock or if any person makes a tender offer for

target's bylaws that institute staggered boards or supermajority voting requirements,³²⁰ sales of shares to a "white squire,"³²¹ and acquisitions of other companies to create antitrust or regulatory roadblocks for tender offerors³²²—are, in general, presumptively manipulative.³²³ Of course, because section 14(e) requires

the stock of the target in excess of a certain percentage. The "flip-over" provision entitles the target shareholders to purchase stock of the tender offeror (at a price which is usually one-half of the market price) if the offeror merges the target into itself in a second-step "squeeze-out" merger. The board of directors usually reserves the power to redeem the "rights."

320 A "shark repellent" amendment instituting a staggered board might provide, for example, that only one-third of the board may be elected each year, and as a result a hostile offeror that acquired a majority of the target's shares might have to wait for a least three years to elect a majority of the directors. A "shark repellent" amendment instituting supermajority voting requirements might provide, for example, that 80% of the corporation's shareholders must approve a merger, and consequently, a hostile offeror intending to consummate a second-step "squeeze-out" merger might be unable to obtain the required shareholder approval for the merger.

Under the corporation law of many states, the board of directors has the power to adopt amendments to the bylaws, but there may be legal restrictions on implementing these amendments when they require a supermajority vote of shareholders. Nonetheless, the boards of many companies may conclude that the imperfect protection of such shark repellent amendments is adequate to defend against an outstanding hostile offer. See 1 R. WINTER, M. STUMPF & G. HAWKINS, *SHARK REPELLENTS AND GOLDEN PARACHUTES: A HANDBOOK FOR THE PRACTITIONER* § 1.4, at 11 (Supp. 1988).

321 A "white squire" is a person believed to be friendly to target management, and the term is used in takeover jargon in contrast to a "white knight," who acquires the target company by way of tender offer or merger.

322 See *Panter v. Marshall Field & Co.*, 646 F.2d 271 (7th Cir. 1981) (the target acquired stores in direct competition with the tender offeror and then filed an antitrust action to enjoin the proposed tender offer); Sidak, *Antitrust Preliminary Injunctions in Hostile Tender Offers*, 30 U. KAN. L. REV. 491 (1982). The target's acquisition of a company that is in a regulated industry will create regulatory obstacles for the tender offeror because the acquisition of the target by the offeror will require the approval of a regulatory agency which will delay and perhaps even preclude the acquisition by the offeror.

323 Target companies often purchase their own securities to defeat a third-party tender offer. See *supra* note 105 and accompanying text. Although aware of this practice, Congress neither explicitly outlawed nor permitted it. *SEC v. Carter Hawley Hale Stores*, 760 F.2d 945, 949 (9th Cir. 1985). *But cf.* S. REP. NO. 550, *supra* note 5, at 5 (indicating that Congress did not believe that issuer repurchase programs were undertaken for a legitimate purpose if they were used by management "to preserve or strengthen control by counteracting tender offers" or "to increase the price of the company's shares"). Publicly announced defensive open market repurchase programs, however, unfairly coerce target shareholders to reject the hostile bid and sell in the market to the target. See Bradley & Rosenzweig, *Defensive Stock Repurchases*, 99 HARV. L. REV. 1378, 1393-99, 1401-06 (1986). Accordingly, these defensive repurchase programs should be banned by § 14(e) as a manipulative practice in connection with a tender offer. Congress' delegation of rulemaking power to the SEC in § 13(e) to regulate a corporation's purchase of its own securities does not preclude the application of § 14(e) to defensive repurchases. *Cf.* Bradley & Rosenzweig, *supra*, at 1403-04 (arguing that the SEC's disclosure-oriented approach in rule 13e-1, 17 C.F.R. § 240.13e-1 (1990), to regulating defensive repurchases is

that the prohibited acts occur "in connection with" a tender offer, the section would cover a manipulative defensive measure only if it takes effect, or is adopted, during an outstanding offer.³²⁴

Some defensive tactics are not "manipulative acts" within the meaning of section 14(e). Defensive merger proposals, for example, are generally not manipulative because they provide target shareholders with an additional choice. Also, "leg-up" stock options granted by a target's board to a tender offer contestant in order to encourage competitive bidding in an auction for the target's shares³²⁵ are not manipulative since they enhance the prospects of target shareholders.³²⁶ Although the line between manipulative and nonmanipulative defensive tactics may not always be bright, the test that Congress envisioned is plain: action taken by a target's board in connection with a tender offer is manipulative conduct in violation of section 14(e) if it inhibits the fair exercise of the target shareholders' right to make a choice.

C. *The Validity of Defensive Tactics After Schreiber*

By cutting back the substantive coverage of the Williams Act, *Schreiber* continued the erosion of the Act that *Piper* had started. In *Piper*, the Burger Court trimmed both the class of parties that could sue under the Act and the remedies that were available

inadequate and that the SEC should prescribe means for preventing the substantial pressure that publicly announced defensive open market repurchases exert on target shareholders).

324 For example, a "shark repellent" bylaw provision that is adopted by a putative target company before a tender offer is launched would not be covered by § 14(e). It should be noted, however, that the SEC believes that § 14(e) applies whenever a bidder takes "substantial steps" to commence a tender offer. See rule 14e-3, 17 C.F.R. § 240.14e-3 (1990). A "flip-over" provision of a "poison pill" (see *supra* note 319) that is adopted before a tender offer is commenced (and which necessarily takes effect after the offer is terminated) may be covered by § 14(e) if it can be shown that the offeror requested the target's board to redeem the "poison pill" and the board refused. The failure of the board to redeem is a "manipulative" act within the meaning of § 14(e).

325 A "leg-up" stock option refers to an option to purchase target shares equal to 15% to 20% of the number of shares outstanding. This type of option provides a sufficient incentive to attract a bidder because it not only gives the bidder a "leg up" but also it allows the bidder to purchase a sizable block of stock which can usually be sold at a profit to cover costs in the event that the offer does not succeed. A "lock-up" option, however, might give a "white knight" the right to purchase target shares equal to 100% to 200% of the number of shares outstanding, thereby assuring the "white knight" enough votes to block a second-step "squeeze-out" merger by a hostile bidder.

326 If "leg-up" stock options had existed in 1968, the Williams Act Congress would certainly have found them acceptable. The legislative history clearly indicates that Congress did not want to deny shareholders the opportunities that result from competitive bidding for the target's stock. See *supra* note 48.

when suit was permissible; then in *Schreiber*, the Burger Court severely limited the grounds for suit. Most important, *Schreiber* ruled out the possibility of challenging the validity of defensive tactics under the Act. As a result of this vacuum created by *Schreiber* at the federal level, parties aggrieved by the defensive actions taken by a target company to resist a hostile offer have been forced to turn exclusively to state law.

Both before and after *Schreiber*, the judiciary has been willing to entertain suits questioning the legality of defensive measures under state law.³²⁷ In general, these suits have been based on allegations that the directors of the target company, in adopting defensive strategies, breached their fiduciary duties of care or loyalty owed to the corporation and its shareholders under state corporation law.³²⁸ Instituted by offeror-shareholders or other shareholders of the target company, these actions have sought to enjoin the defenses or to impose liability for damages upon the directors who adopted them.³²⁹

Prior to *Schreiber*, state-law litigation challenging the decisions made by the board of directors of the target company in responding to a hostile offer was usually unsuccessful. After a nominal scrutiny of the record, the courts held that the plaintiffs had not produced sufficient evidence to overcome the protections and presumption of the so-called business judgment rule.³³⁰ Under

327 See D. BLOCK, N. BARTON & S. RADIN, *THE BUSINESS JUDGMENT RULE*, app. A at 627-41 (3d ed. 1989) [hereinafter BLOCK, BARTON & RADIN] (citing all cases in which the validity of defensive tactics have been challenged under state law).

328 See cases cited in *id.*; cf. *Revlon, Inc. v. MacAndrews & Forbes Holdings*, 506 A.2d 173, 179 (Del. 1986) (indicating that the fiduciary duties of care and loyalty in Delaware are "the bedrock of [the] law regarding corporate takeover issues"). The duty of care "refers to the responsibility of a corporate fiduciary to exercise, in the performance of his tasks, the care that a reasonably prudent person in a similar position would use under similar circumstances." *Norlin Corp. v. Rooney, Pace, Inc.*, 744 F.2d 255, 264 (2d Cir. 1984). The duty of loyalty is "transgressed when a corporate fiduciary . . . uses his or her corporate office . . . to promote, advance or effectuate a transaction between the corporation and such person . . . and that transaction is not substantively fair to the corporation." *Solash v. Telex Corp.*, [1987-1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,608, at 97,727 (Del. Ch. 1988). The duties of care and loyalty are based on common-law principles, but today most states impose these duties by statute. See BLOCK, BARTON & RADIN, *supra* note 327, at 2, app. C at 653-71 (selected state statutes imposing a duty of care), app. E at 691-715 (selected state statutes imposing a duty of loyalty). The governing law is the law of the state where the target company is incorporated. See *id.* at 2 (citing cases).

329 See cases cited in BLOCK, BARTON & RADIN, *supra* note 327, at 627-41.

330 See, e.g., *Jewel Cos. v. Pay Less Drug Stores Northwest*, 741 F.2d 1555 (9th Cir. 1984); *Gearhart Indus. v. Smith Int'l, Inc.*, 741 F.2d 707 (5th Cir. 1984); *Buffalo Forge Co. v. Ogden Corp.*, 717 F.2d 757 (2d Cir.), *cert. denied*, 464 U.S. 1081 (1983); *Panter v.*

this common-law rule, a court will not evaluate the wisdom or fairness of a decision of the directors unless the plaintiff is able to come forward with evidence demonstrating that the directors did not follow a deliberative process in reaching the decision or that the decision was made by a predominately interested board with an interest in the decision adverse to the corporation.³³¹ In other words, the business judgment rule creates a presumption that directors have acted with due care and undivided loyalty in making a business decision, and, as such, the rule is a tool of judicial review.³³²

As the efficacy of federal review of defensive measures was waning, the judiciary began to recognize that the standard of review under state law was too lax; and after *Schreiber* sounded the death knell for federal review, judicial recognition of the inadequacy of state law intensified. In the main, the courts realized that sometimes directors do not carefully evaluate all relevant information in adopting a defensive strategy or that directors may resist a hostile offer in order to entrench themselves in office. Because of this omnipresent specter of ill-conceived or self-interested defensive tactics, the courts concluded that the business judgment rule, as it had been applied, afforded directors too much latitude in devising strategies to resist unfriendly advances. As a consequence, courts have modified the manner in which they apply the business judgment rule in corporate control transactions.³³³ There is no general accord, however, on what modifi-

Marshall Field & Co., 646 F.2d 271 (7th Cir.), *cert. denied*, 454 U.S. 1092 (1981); Treadway Cos. v. Care Corp., 638 F.2d 357 (2d Cir. 1980); Crouse-Hinds Co. v. InterNorth, Inc., 634 F.2d 690 (2d Cir. 1980), *cert. denied*, 450 U.S. 999 (1981). It should be recalled, however, that in suits challenging the validity of defensive tactics under § 14(e) prior to *Sante Fe Indus. v. Green*, 430 U.S. 462 (1977), the federal courts ruled—without mentioning the business judgment rule—that the directors' adoption of a defensive tactic for no valid business purpose was a breach of fiduciary duty under state law and that this fiduciary misconduct translated into a violation of § 14(e). See *supra* text accompanying note 222.

331 See generally BLOCK, BARTON & RADIN, *supra* note 327, at 1-90 (discussing the business judgment rule and its relationship to the duty of care and duty of loyalty). The business judgment rule, which recognizes that courts have limited competence to assess business decisions, is a nonstatutory equitable doctrine that is applied by the courts on a case-by-case basis.

332 See *id.* at 2-3, 8-10.

333 See Brennan, *New Cases on the Business Judgment Rule: Defending Defensive Tactics Becomes More Difficult*, 14 SEC. REG. L.J. 245 (1986); Veasey, *Further Reflections on Court Review of Judgments of Directors: Is the Judicial Process Under Control?*, 40 BUS. LAW. 1373 (1985); Wander & LeCoque, *Boardroom Jitters: Corporate Control Transactions and Today's Business Judgment Rule*, 42 BUS. LAW. 29 (1986); Note, *Corporate Auctions and Directors'*

cations are appropriate.³³⁴ Significantly, the Court of Appeals for the Second Circuit, applying New York law, and the Supreme Court of Delaware are in disagreement over the proper approach.³³⁵

The Second Circuit continues to adhere to the traditional business judgment rule but has relaxed the plaintiff's burden in rebutting the presumption of the rule. The court scrutinizes the record more closely for evidence indicating that the directors were not fully informed or that they were acting primarily in their own interests. And if the court is satisfied that there is sufficient evidence suggesting fiduciary misconduct, the burden shifts to the directors to justify the wisdom or fairness of their actions. As a practical matter, directors have been hard-pressed to justify their actions under this rigorous standard of review. Therefore, whenever a court invokes this standard, the plaintiff is usually granted the requested relief.³³⁶

Fiduciary Duties: A Third-Generation Business Judgment Rule, 87 MICH. L. REV. 276 (1988). Legal commentators disagree on whether the common-law business judgment rule has been strained by its application in the takeover context or whether it has been resilient. Compare Brennan, *supra* (arguing that the business judgment rule is being used by default) with Veasey, *supra* (arguing that the business judgment rule consistently leads to logical and enduring answers).

334 See Wander & LeCoque, *supra* note 333, at 31-38.

335 The Second Circuit and the Supreme Court of Delaware also differ on the standard of culpability—ordinary negligence or gross negligence—required for the grant of equitable relief in suits alleging a breach of the duty of care. In *Hanson Trust PLC v. ML SCM Aquisition, Inc.*, 781 F.2d 264, 275 (2d Cir. 1986), the Second Circuit, applying New York law, ruled that directorial conduct that “did not rise to the level of gross negligence” still constituted a breach of the duty of care for purposes of injunctive relief. In contrast, in *Moran v. Household Int'l Inc.*, 500 A.2d 1346, 1356 (Del. 1985)—a suit also seeking injunctive relief—the Supreme Court of Delaware utilized gross negligence as the standard of culpability. Controversy regarding the standard of culpability required for the imposition of liability for damages for a breach of the duty of care has been partially mooted by the enactment in Delaware, New York, and 36 other states of provisions authorizing the adoption by shareholders of charter provisions eliminating or limiting the liability of directors (but not officers) for damages for breaches of the duty of care. All of these statutory provisions have been enacted since 1985. See BLOCK, BARTON & RADIN, *supra* note 327, at 40-48, app. D at 673-88 (citing all such statutes and setting forth selected provisions); see also Veasey, Finkelstein & Bigler, *Delaware Supports Directors with a Three-Legged Stool of Limited Liability, Indemnification, and Insurance*, 42 BUS. LAW. 399 (1987).

336 See *Hanson Trust*, 781 F.2d at 272 (2d Cir. 1986) (granting a preliminary injunction after stating that “the district court erred in holding that [the plaintiff] failed to make a prima facie showing of a breach of a fiduciary duty [of care]” and that “once the burden shifted, the extensive evidence presented . . . clearly show[ed] that . . . the [directors] did not sustain their burden justifying the fairness of the lock-up option”); *Norlin Corp. v. Rooney, Pace, Inc.*, 744 F.2d 255, 265 (2d Cir. 1984) (granting a preliminary injunction after stating that “once self-dealing . . . is demonstrated, the duty of

Cognizant that there is a fundamental tension between the lenient business judgment rule and the stringent wisdom-or-fairness test and that a choice of either standard in reviewing the conduct of directors is frequently determinative of the outcome of the litigation, the Delaware Supreme Court announced in 1985 that it would apply an intermediate form of review in suits challenging the directors' adoption of a defensive measure.³³⁷ This new standard places the initial burden on the directors to prove (1) that they had "reasonable grounds for believing that a danger to corporate policy and effectiveness existed," a burden that can be sustained by a showing of good faith and reasonable investigation, and (2) that the defensive measure adopted by the board was "reasonable in relation to the threat posed."³³⁸ Once the court is satisfied that the directors have fulfilled their basic duties of care and loyalty under this test, the directors are entitled to the normal protections of the business judgment rule.³³⁹ Al-

loyalty supersedes the duty of care, and the burden shifts to the directors to [prove the fairness of "white squire" stock transactions] and that "[i]n this case, the evidence adduced was more than adequate to constitute a prima facie showing of self-interest" and the directors "failed to demonstrate [that their actions were fair]". California seems to follow the approach taken by the Second Circuit. See *Heckmann v. Ahmanson*, 168 Cal. App. 3d 119, 128, 214 Cal. Rptr. 177, 183 (1985) (ruling that evidence of an effort by the board to retain control is sufficient to shift the burden to the directors to demonstrate the inherent fairness of the transaction).

337 See *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985); see also *Gilson & Kraakman, Delaware's Intermediate Standard for Defensive Tactics: Is There Substance to Proportionality Review?*, 44 BUS. LAW. 247, 248, 250 (1989) (stating that "[t]he evolutionary trajectory of [the] proportionality test is far from certain" but that Delaware adopted the test because of "[a]n outpouring of academic commentary call[ing] for constraints on defensive tactics" and because "it even appeared possible that Congress might act to displace state law—especially Delaware law—that was unduly favorable to target management").

338 *Unocal*, 493 A.2d at 955. In litigation stemming from the *Schreiber* case, *Gilbert v. El Paso Co.*, 575 A.2d 1131 (Del. 1990), the Supreme Court of Delaware applied the *Unocal* test. Delaware's *Unocal* test has been relied upon by courts construing the law of other states. See, e.g., *International Ins. Co. v. Johns*, 874 F.2d 1447, 1458-59 (11th Cir. 1989) (Florida law); *Amanda Acquisition Corp. v. Universal Foods Corp.*, 708 F. Supp. 984, 1009 (E.D. Wis.), *aff'd on other grounds*, 877 F.2d 496 (7th Cir. 1989) (Wisconsin law); *Torchmark Corp. v. Bixby*, 708 F. Supp. 1070, 1081 (W.D. Mo. 1988) (Missouri law); *Gelco Corp. v. Coniston Partners*, 652 F. Supp. 829, 845 (D. Minn. 1986), *aff'd on other grounds*, 811 F.2d 414 (8th Cir. 1987) (Minnesota law). But see *A. Copeland Enters. v. Guste*, 706 F. Supp. 1283, 1290 n.15 (W.D. Tex. 1989) (distinguishing *Unocal* from Texas law). Some states, such as Indiana and Ohio, have enacted legislation that specifically rejects the *Unocal* test, and therefore the ordinary business judgment rule is used in the corporate control context. See IND. CODE ANN. § 23-1-35-1(f) (West Supp. 1990); OHIO REV. CODE ANN. § 1701.59(C)(1) (Anderson Supp. 1990).

339 *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1288 (Del. 1989). Once the directors receive the benefit of the business judgment rule, the burden shifts to the

though Delaware's refinement of the business judgment rule eliminates the blanket protection of defensive tactics that generally existed under prior Delaware law,³⁴⁰ it does not foreclose the adoption of defensive maneuvers that have a coercive or preclusive effect on shareholder choice.³⁴¹

plaintiffs who have the ultimate burden of persuasion to show a breach of fiduciary duty. *Moran v. Household Int'l*, 500 A.2d 1346, 1356 (Del. 1985). If the directors do not satisfy both prongs of the *Unocal* test, the directors lose the benefit of the business judgment rule, and they must demonstrate the fairness of the transaction. *Macmillan*, 559 A.2d at 1280. Since the plaintiff must only demonstrate a reasonable probability of success on the merits in suits seeking a preliminary injunction, a failure of the directors to satisfy both prongs of the *Unocal* test usually means that the plaintiff will be able to demonstrate a reasonable likelihood of prevailing on the merits and that the injunction will be granted. See *AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103, 114-15 (Del. Ch. 1986).

340 See *Macmillan*, 559 A.2d at 1261 (granting preliminary injunctive relief invalidating a "lock-up" option after having found a breach of the duties of care and loyalty); *Revlon, Inc. v. MacAndrews & Forbes Holdings*, 506 A.2d 173 (Del. 1986) (same).

341 See *Paramount Communications v. Time, Inc.*, 571 A.2d 1140 (Del. 1990) (denying a request to enjoin several preclusive defensive measures having found that the measures were a reasonable and proportionate response to a perceived threat); *Moran v. Household Int'l, Inc.*, 500 A.2d 1346 (Del. 1985) (denying a request to enjoin a "poison pill" having found that its adoption was a reasonable and proportionate response to a perceived threat, but indicating that if the directors subsequently refused a request to redeem the "poison pill," their refusal would be subject to review under the same standard that was applied in evaluating the propriety of adoption). But see *Dynamics Corp. of Am. v. CTS Corp.*, 794 F.2d 250 (7th Cir. 1986) (granting a preliminary injunction against a "poison pill" under Indiana law, after indicating that Indiana would apply Delaware's *Unocal* test [that is, until the Indiana legislature specifically rejected it, see *supra* note 338]), *rev'd on other grounds*, 481 U.S. 69 (1987).

In a line of cases decided after the Delaware Supreme Court's decision in *Unocal*, the court fleshed out the director's *Unocal* duties in responding to a hostile offer. First, directors may refuse to entertain an offer (the so-called "Just Say No" defense). *Macmillan*, 559 A.2d at 1285. Second, in determining whether a hostile offer poses a threat to corporate policy and effectiveness so that a defensive measure may be adopted, the directors may take into account the coercion from a two-tier offer, an inadequate price, shareholder confusion, loss of strategic benefits, and the uncertain aspects of the offer. *Time*, 571 A.2d at 1152-53. Third, while there is no per se duty to maximize shareholder value in the short term, once a break-up of the target company is inevitable, the directors have a duty either to auction the company or to maximize short-term shareholder value (the so-called "*Revlon* duties"). *Revlon*, 506 A.2d at 184-85. Last, once the target is in a "*Revlon* mode," the directors may treat one or more of the bidders on unequal terms as long as they properly perceive that shareholders' interests are enhanced by this disparate treatment. *Macmillan*, 559 A.2d at 1288. For a discussion of the relationship among *Time*, *Unocal*, and *Revlon*, see generally Johnson & Millon, *The Case Beyond Time*, 45 BUS. LAW. 2105 (1990) (observing that *Time* may signal the demise of *Unocal* and raises questions about the "normative basis" of *Revlon*). For a differing view, see Note, *Time and Time Again the Board is Paramount: The Evolution of the Unocal Standard and the Revlon Trigger Through Paramount v. Time*, 66 NOTRE DAME L. REV. 159 (1990) (concluding that, after *Time*, *Unocal* and *Revlon* are alive and well but appropriately limited to a non-substantive, threshold test application for determining the applicability of the business judgment rule).

The courts' efforts in tailoring the business judgment rule to the corporate control context have not been in vain, since most of the commonly employed defensive tactics have been challenged under state law in the post-Schreiber era. Yet, except for the consistent validation of "leg-up" stock options,³⁴² a consensus has not been reached on which defenses are legal and which are not. For example, "lock-up" options, "poison pills," "shark repellent" bylaw provisions, and "white squire" stock transactions have withstood judicial examination in some cases and have been enjoined in others.³⁴³

D. *The Validity of Offensive Strategies After Schreiber*

The courts, the SEC, and commentators have recognized that bidders often structure their tender offers so that target shareholders are unfairly coerced to tender their shares.³⁴⁴ And there is no gainsaying that target companies adopt coercive and preclusive defensive tactics in many takeover battles primarily to counteract these structurally coercive offers.³⁴⁵ The prototype of a

³⁴² See, e.g., *Buffalo Forge Co. v. Ogden Corp.*, 717 F.2d 757 (2d Cir.), *aff'g* 555 F. Supp. 892 (W.D.N.Y.), *cert. denied*, 464 U.S. 1018 (1983); *Hastings-Murtagh v. Texas Air Corp.*, 649 F. Supp. 479 (S.D. Fla. 1986).

³⁴³ Defensive tactics have been declared valid in, *Cottle v. Storer Communication*, 849 F.2d 570 (11th Cir. 1988) ("lock-up" option); *Treco, Inc. v. Land of Lincoln Sav. & Loan*, 749 F.2d 374 (7th Cir. 1984) ("shark repellent", *pre-Schreiber*); *Desert Partners v. USC Corp.*, 686 F. Supp. 1289 (N.D. Ill. 1988) ("poison pill"); *CRTF Corp. v. Federated Dep't Stores*, 683 F. Supp. 422 (S.D.N.Y. 1988) ("poison pill"); *Shamrock Holdings v. Polaroid Corp.*, 559 A.2d 278 (Del. Ch. 1989) ("white squire" transaction); *Moran v. Household Int'l*, 500 A.2d 1346 (Del. 1985) ("poison pill"). Defensive tactics have been enjoined in, *Dynamics*, 794 F.2d 250 ("poison pill"); *Hanson Trust PLC v. ML SCM Acquisition, Inc.*, 781 F.2d 264 (2d Cir. 1986) ("lock-up" option); *Norlin v. Rooney, Pace, Inc.*, 744 F.2d 255 (2d Cir. 1984) ("white squire" transaction, *pre-Schreiber*); *Buckhorn, Inc. v. Ropak Corp.*, 656 F. Supp. 209 (S.D. Ohio), *aff'd mem.*, 815 F.2d 76 (6th Cir. 1987) ("white squire" transaction); *R.D. Smith & Co. v. Preway Inc.*, 644 F. Supp. 868 (W.D. Wis. 1986) ("poison pill"); *Macmillan*, 559 A.2d 1261 ("lock-up" option); *Reulon*, 506 A.2d 173 ("lock-up" option); *Datapoint Corp. v. Plaza Sec. Co.*, 496 A.2d 1031 (Del. 1985) ("shark repellent"); *Blasins Indus. v. Atlas Corp.*, [1988-1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,965 (Del. Ch. July 25, 1988) ("shark repellent").

³⁴⁴ See, e.g., *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1152 (Del. 1990); *Moran v. Household Int'l, Inc.*, 500 A.2d 1346, 1357 (Del. 1985); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 956 (Del. 1985); *City Capital Assocs. v. Interco, Inc.*, 551 A.2d 787, 797 (Del. Ch.), *appeal dismissed*, 556 A.2d 1070 (Del. 1988); *Eisenberg v. Chicago Milwaukee Corp.*, 537 A.2d 1051, 1056 (Del. Ch. 1987); Notice of Possible Action Regarding Two-Tier Tender Offer Pricing and Non-Tender Offer Purchase Programs, Exchange Act Release No. 21,079, [1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,637, at 86,916-18 (June 21, 1984); *Bebchuk, The Pressure to Tender: An Analysis and a Proposed Remedy*, 12 DEL. J. CORP. L. 911, 911 n.1 (1987) (citing articles by practicing lawyers, legal academics, and economists that discuss the problem); *cf. infra* note 454.

³⁴⁵ See Lipton, *Corporate Governance in the Age of Finance Corporatism*, 136 U. PA. L.

structurally coercive offer is the front-end loaded, two-tier offer.³⁴⁶ The terms of such an offer provide that target shareholders who do not tender into the front-end tender offer will be squeezed out in the back-end merger at a lower price. Rational target shareholders faced with this type of offer are pressured to tender even if they believe that the tender offer price is inadequate.³⁴⁷ Because of its coercive effect on shareholder decisionmaking, should be barred by section 14(e) of the Williams Act as a front-end loaded offer as a manipulative tender offer practice. As was the case with defensive tactics, however, *Schreiber* foreclosed this argument since the terms of a front-end loaded offer are fully and fairly disclosed.³⁴⁸ And unlike defensive tactics, a front-end loaded offer cannot be challenged under the state law pertaining to misconduct by a corporate fiduciary, because at the time such an offer is made the bidder does not have a fiduciary relationship (as a controlling shareholder) with the target company or its shareholders.³⁴⁹ Moreover, if the tender offer is successful in producing control so that the back-end merger can be consummated, the lot of the minority shareholders who are squeezed out in the merger is not a happy one. In light of the Supreme Court's opinion in *Santa Fe*, the substantive fairness of the merger cannot be questioned under the federal securities laws. An appraisal remedy based on the market price of the target's shares before the offer may be the minority shareholders' exclusive remedy under state law.³⁵⁰

REV. 1, 28 (1987) (arguing that although defensive tactics limit the investment choices of target shareholders and "may be undesirable in the abstract," they are nonetheless "legitimate responses to abusive takeover schemes").

346 Cf. Bebchuk, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 HARV. L. REV. 1695, 1717-35 (1985) (arguing that partial offers and any-or-all offers without a squeeze-out commitment have the same coercive effect on shareholder choice as front-end loaded, two-tier offers).

347 See Comment, *Judicial Review of Antitakeover Devices Employed in the Noncoercive Tender Offer Context: Making Sense of the Unocal Test*, 138 U. PA. L. REV. 225, 228 n.20 (1989).

348 See *Radol v. Thomas*, 772 F.2d 244, 255 (6th Cir. 1985) (holding, in reliance on *Schreiber*, that a front-end loaded, two-tier offer was not "manipulative" within the meaning of § 14(e)), *cert. denied*, 977 U.S. 903 (1986); see also *Martin Marietta Corp. v. Bendix Corp.*, 549 F. Supp. 623 (D. Md. 1982) (pre-*Schreiber* case holding, in reliance on *Piper* and *Santa Fe*, that a front-end loaded, two-tier "Pac-Man" defensive offer was not "manipulative" within the meaning of § 14(e)).

349 See *Osofsky v. J. Ray McDermott & Co.*, 725 F.2d 1057, 1060 (2d Cir. 1984); *Gilbert v. El Paso Co.*, 490 A.2d 1050, 1055-56 (Del. Ch. 1984), *aff'd*, 575 A.2d 1131 (Del. 1990); Weiss, *supra* note 233, at 1108.

350 See *supra* text accompanying notes 227-31; Bebchuk, *supra* note 344, at 917-18;

Bidders have also been able to facilitate the success of their takeover attempts by revoking an initial tender offer and then launching a second tender offer on different terms (as Burlington did in its takeover of El Paso)³⁵¹ or "sweeping the street" through privately negotiated or open market purchases.³⁵² A bidder's revocation of a tender offer is not a "manipulative" act within the meaning of section 14(e). It does not unfairly coerce or prevent the investment decisions of target shareholders, and as *Schreiber* correctly held, it is not an artificial practice designed to deceive target shareholders. But as the appellate court opinion in the *Schreiber* litigation suggested, a withdrawal of a tender offer may constitute a breach of contract that is actionable by target shareholders who tendered into the offer before it was withdrawn.³⁵³

The law governing the contractual rights and obligations of a tender offeror and target shareholders is a blend of state contract law and Williams Act corporation law and can be summarized as follows:³⁵⁴ A tender offer is usually an offer for a unilateral con-

Lipton, *supra* note 345, at 18-19; *cf. supra* note 231.

351 See *supra* text following note 239.

352 "Street sweeps" are possible in this situation because the market dynamics that result from the announcement of the initial tender offer allow arbitrageurs and broker-dealers to assemble large blocks of the target's stock which the bidder then purchases immediately after it revokes the tender offer. (While the offer is still open, rule 10b-13, 17 C.F.R. § 240.10b-13 (1990), prohibits the bidder from purchasing the target's stock outside the offer. See *supra* note 282.) Hanson Trust used this strategy in its takeover of SCM Corporation in 1985. *Hanson Trust PLC v. SCM Corp.*, 774 F.2d 47, 50-53 (2d Cir. 1985). In *Hanson Trust*, the court ruled that Hanson Trust's acquisition of 25% of SCM Corporation's stock through five private purchases from sophisticated professionals and one open market purchase, within hours after it had revoked its earlier tender offer for any or all of SCM Corporation's stock, did not amount to a new tender offer or a continuation of the one it had withdrawn. Hence, the court held that Hanson Trust's privately negotiated and open market purchases were not subject to the tender offer provisions of the Williams Act. *Id.* at 57. Troubled by the decision in *Hanson Trust*, the SEC published for comment a proposed rule that prohibits substantial "street sweeps" by a bidder for 30 business days after a tender offer is revoked. See Proposed Rule Regarding Acquisitions of Substantial Amounts of Securities During and Following a Tender Offer, Exchange Act Release No. 24,976, [1987 Transfer Binder] Fed. Sec. L. Rep. (CGH) ¶ 84,160 (Oct. 1, 1987). The proposed rule has never been adopted. For a discussion of the issue by legal commentators, see Andre, *Unconventional Offers Under the Williams Act: The Case for Judicial Restraint*, 11 J. CORP. L. 499 (1986); Segre, *Open-Market and Privately Negotiated Purchase Programs and the Market for Corporate Control*, 42 BUS. LAW. 715 (1987); Tyson, *The Williams Act After Hanson Trust v. SCM Corporation: Post-Tender Offer Purchases by the Tender Offer*, 61 TUL. L. REV. 1 (1986); Note, *Proposed SEC Regulation of Market Sweeps: Should Market Sweeps Be Governed by the Williams Act?*, 56 FORDHAM L. REV. 797 (1988); Note, *Post-Tender Offer Purchases: Rebalancing the Scales*, 65 TEX. L. REV. 185 (1986).

353 See *supra* text accompanying note 244.

354 Cf. DeMott, *Current Issues in Tender Offer Regulation: Lessons from the British*, 58

tract which target shareholders can accept by tendering their shares.³⁵⁵ Therefore, a mutually enforceable contract is formed at the time of tender. Yet, by dint of their withdrawal rights under the Williams Act, target shareholders have an absolute right to rescind this contract during the withdrawal period specified in the Act or by SEC rule.³⁵⁶ Although the bidder does not have a corresponding right to undo the tender offer contract, the bidder's obligation under the contract may be extinguished as a matter of basic contract law if the offer provides that the obligation to purchase tendered shares will be discharged upon the happening of a future event (over which the bidder has no control) and that event does in fact take place.³⁵⁷ In practice, most

N.Y.U. L. REV. 945, 970 (1983) (pointing out that a tension exists between the traditional common law of contracts and the Williams Act provisions).

355 *Lowenschuss v. Kane*, 520 F.2d 255, 264 (2d Cir. 1975); *Gilbert v. El Paso Co.*, 490 A.2d 1050, 1054 (Del. Ch. 1984), *aff'd*, 575 A.2d 1131 (Del. 1990). *But see* Lowenstein, *supra* note 210, at 498 & n.34 (suggesting that the contract between the bidder and a tendering target shareholder is analogous to an "at-will" contract that may be terminated by either party at any time without liability). It should also be noted that section 14(d) of the Williams Act contemplates that a bidder, instead of making a tender offer, may make "a request or invitation for tenders." If the bidder proceeds in this fashion, it is arguable that the bidder is not an "offeror" under basic contract law and that the bidder must accept the tenders by target shareholders for a contract to be formed. *But see Lowenschuss*, 520 F.2d at 265 n.9 (rejecting the suggestion of the district court that a tender offer is an "offer for an offer").

356 *See* Proposed Tender Offer Rule and Schedule, Exchange Act Release No. 15,548, *supra* note 56, at 81,228 n.87 (citing E. ARANOW & H. EINHORN, *supra* note 3, at 134). The right of target shareholders to rescind the contract does not cause their acceptances to be considered "illusory," and the bidder's duty to perform under the contract, therefore, is not affected by the existence of this right.

357 *See Lowenschuss v. Kane*, 520 F.2d at 264-65; *Gilbert*, 490 A.2d at 1054, *aff'd*, 575 A.2d 1131 (Del. 1990). A bidder's obligation under the contract would be partially discharged, for example, if the offer provided that the bidder was not willing to purchase more than a certain number of shares and more than that number was tendered. An offer may also provide that the bidder's obligation under the contract will not mature if a certain event (such as the deposit of a minimum number of shares) does not occur. If the offer is made conditional but none of the conditions occur, the bidder presumably may still withdraw the offer as to shareholders who have not yet tendered. If the bidder intends to go through with the offer, however, it must keep the offer open for at least 20 business days. *See* rule 14e-1(a), 17 C.F.R. § 240.14e-1(a) (1990) (establishing the minimum offering period for third-party offers); rule 13e-4(f), 17 C.F.R. § 240.13e-4(f)(1) (establishing the minimum offering period for issuer offers); *supra* text accompanying notes 96 & 106-08. Rule 13e-4 acknowledges that offers may be "withdrawn," but rule 14e-1 curiously does not.

Prior to 1986, the SEC's approach to tender offer regulation was generally consistent with the preceding explanation. Significantly, the SEC took the position that if the terms of an offer "permit[ted] the bidder to unilaterally terminate [the] offer," the bidder was allowed to decrease the consideration offered or the amount of securities sought upon returning all tendered shares and commencing a new offer. Proposed Amendments

tender offers contain such an "out" clause, and the bidder reserves the right to revoke the offer (as Burlington did) if any of the "conditions out" occur.³⁵⁸

E. The Validity of the SEC's Tender Offer Rules After Schreiber

The Supreme Court in *Schreiber* stressed that *all three* species of tender offer misconduct outlawed by section 14(e)—fraudulent, deceptive, and manipulative practices—required some element of misrepresentation or nondisclosure.³⁵⁹ The Court was also insistent about the significance of the 1970 amendment to section 14(e), which gave the SEC authority to define practices forbidden by section 14(e) and prescribe means reasonably designed to prevent them.³⁶⁰ The Court emphasized that this amendment suggested no change in the meaning of the words "fraudulent," "deceptive," or "manipulative" and, therefore, SEC prophylactic rulemaking under section 14(e) was limited to guarding against conduct that involved misrepresentation or nondisclosure.³⁶¹ The Court was not as unequivocal about the scope of the SEC's prophylactic rulemaking power under section 13(e) and actually expressed facially conflicting thoughts regarding the legislative purpose of the provision.³⁶² But since section 13(e) and section 14(e) contain virtually identical language, it seems appropriate, on balance, to conclude that the Court believed that the SEC's

Regarding Equal Treatment of Target Shareholders, Exchange Act Release No. 22,198, *supra* note 86, at 87,563 & n.16. In 1986, when withdrawal rights were extended to the life of the offer, the SEC reversed its position and indicated that a bidder could decrease the consideration offered or the percentage of securities sought without commencing a new offer. Adoption of All-Holders and Best-Price Rule, Exchange Act Release No. 23,421, *supra* note 83, at 88,187; *see also supra* note 87. This position suggests that a contract is not formed until the expiration of the tender offer; and if the formation of the tender offer contract occurs at expiration, withdrawal rights add nothing to the rights target shareholders already have under contract law. If a bidder decreases the price of an offer and shareholders do not have statutory withdrawal rights (because the securities sought in the offer are not registered equity securities), are the shareholders who tendered before the decrease in price still contractually bound to sell their shares?

358 *See supra* note 240 and accompanying text.

359 *See supra* note 253 and accompanying text.

360 *See supra* note 95 and accompanying text.

361 *Schreiber*, 472 U.S. at 11 n.11. The Court only stated that the 1970 amendment to § 14(e) suggested no change in the meaning of the word "manipulative," but it seems certain that the Court also believed that the amendment was meant to effect no change in the meaning of the words "fraudulent" or "deceptive." *Cf. United States v. Chestman*, 903 F.2d 75, 86 (2d Cir.) (Mahoney, J.), *aff'd on rehearing*, No. 89-1276, 1990 US App LEXIS 18175 (2d Cir. 1990) (LEXIS, Genfed library, US App file) (en banc).

362 *See supra* note 256; *supra* text accompanying note 255.

rulemaking power under section 13(e) was subject to the same limitation as the SEC's rulemaking power under section 14(e).³⁶³

As discussed in Part I of this Article, the SEC has promulgated numerous tender offer rules pursuant to its authority under sections 14(e) and 13(e). These rules are somewhat disappointing because they fail to define specifically the practices for which the prophylactic measures are designed, and they never indicate which species of misconduct is at issue.³⁶⁴ Nonetheless, when the rules are parsed, it becomes apparent that they seek to prevent not only practices that involve misrepresentation or nondisclosure but also practices that involve unfair coercion or unequal treatment of target shareholders. As this Article has argued, Congress meant section 14(e) to prohibit both deceptive conduct and nondeceptive unfair conduct. Thus, the SEC's prophylactic rules guarding against both types of conduct are consistent with Congress' intent.³⁶⁵ But in light of *Schreiber*, the judiciary would

363 See Fiffis, *supra* note 256, at 324 (“[L]ower courts certainly should interpret section 13(e)'s language consistently with section 14(e)'s identical language.”).

364 See Swanson, *Federal Regulation of Issuer Tender Offers*, 12 PAC. L.J. 659, 671 (1981) (suggesting that the current definitions in rule 13e-4 are circular and that the SEC should have defined the words “fraudulent,” “deceptive,” and “manipulative” by giving specific examples). Rule 13e-4, as proposed in 1977, did define five specific tender offer practices that were “fraudulent,” “deceptive,” or “manipulative.” See 42 Fed. Reg. 63,069 (Dec. 7, 1977). Two years later, the SEC eliminated these specific definitions in the final version of the rule in order “to obviate concern as to whether the [SEC] had intended to introduce unfamiliar concepts of fraud, deceit and manipulation” and defined the words “fraudulent,” “deceptive,” and “manipulative” in more general, traditional terms as it had done in rule 10b-5, 17 C.F.R. § 240.10b-5 (1990). Adoption of Rules Regarding Tender Offers by Issuers, Exchange Act Release No. 16,112, *supra* note 108, at 82,208. The requirements of the rule, however, remained basically unchanged. See 17 C.F.R. § 240.13e-4 (1990).

365 The legislative history of § 13(e) and the 1970 amendment to § 14(e) reveals that the SEC made members of Congress aware of its belief that the grant of rulemaking authority in §§ 13(e) and 14(e) included the authority to adopt rules designed to prevent unfair substantive conduct. First, the SEC indicated that § 13(e) could be used to adopt rules providing shareholders in issuer offers with substantive protections paralleling those afforded shareholders in tender offers governed by § 14(d). See *Senate Hearings, supra* note 10, at 202 (Supplemental Memorandum of the SEC with Respect to Certain Comments on S. 510); see also Note, *SEC Takeover Regulation Under the Williams Act*, 62 N.Y.U. L. REV. 580, 595 (1987). Second, the SEC provided Congress with a list of examples of fraudulent, deceptive, or manipulative practices used in tender offers that the SEC's rulemaking authority under § 14(e) would be able to prevent. While some of these practices involved a failure to disclose, others involved unfair substantive conduct, such as a bidder's failure to pay promptly for securities purchased or to return promptly securities not purchased and a bidder's failure to have on hand the funds to pay for the securities sought. See *Additional Consumer Protection in Corporate Takeovers and Increasing the Securities Act Exemptions for Small Businessmen: Hearings on S. 3431 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 91st Cong., 2d Sess. 12 (1970)

most likely contend that while the SEC may have followed Congress' mandate when it adopted rules guarding against a failure to disclose, the SEC exceeded the scope of its rulemaking authority in seeking to prevent unfair substantive conduct.

In addition to rule 13e-1³⁶⁶ and the disclosure provisions of rule 13e-4,³⁶⁷ two other provisions stand out as examples of rules that guard against a failure to disclose: rule 14e-2³⁶⁸ and rule 13e-4(f)(6).³⁶⁹ Rule 14e-2 requires a company that is the subject of a tender offer to inform its shareholders of its position regarding the offer. Based on the theory that target management has a duty to disclose its position,³⁷⁰ this rule is designed to avert a fraudulent practice involving nondisclosure: target management's silence as a breach of a duty to disclose. Rule 13e-4(f)(6) prohibits a company from purchasing its shares for ten business days after the company has terminated a tender offer for its shares. The purpose of this restriction is to preclude the company from deceiving investors by artificially pegging the market price of its stock at the inflated tender offer price. Thus, rule 13e-4(f)(6) seeks to prevent price manipulation, which depends on nondisclosure for its success.³⁷¹ Because these rules are predicated on traditional concepts of fraud and manipulation—concepts that received the Court's imprimatur in *Schreiber*—they are valid.

The remainder of the SEC's rules adopted under sections 14(e) and 13(e) seek to prevent unfair practices. By way of summary of rules already touched on, consider the following: First, rule 14e-1³⁷² (in the case of third-party offers) and rule 13e-

(Memorandum Prepared by Division of Corporate Finance); see also Junewicz, *supra* note 233, at 1179-80. Furthermore, the *Schreiber* Court itself suggested that Congress intended to give the SEC the authority under § 14(e) to adopt rules regulating activities that were not outlawed per se by § 14(e) as long as the activities predictably gave rise to conduct that was outlawed. *Schreiber*, 472 U.S. at 11 n.11, and some of the SEC's rules that seek to prevent unfair substantive conduct are of this genre.

366 17 C.F.R. § 240.13e-1 (1990); see *supra* notes 103-04 and accompanying text.

367 17 C.F.R. § 240.13e-4(c)-(e) (1990); see *supra* note 108.

368 17 C.F.R. § 240.14e-2 (1990); see *supra* text following note 95; *supra* text accompanying notes 98-100.

369 17 C.F.R. § 240.13e-4(f)(6) (1990).

370 In the release adopting rule 14e-2, the SEC did not unequivocally state that target management has a duty to disclose its position, but it intimated that such a duty exists by noting the fiduciary nature of the relationship between management and shareholders and by pointing out that management's position "can have a determinative effect on the outcome of a tender offer and thus is material to [shareholders]." Adoption of Amendments to Tender Offer Rules, Exchange Act Release No. 16,384, *supra* note 58, at 82,599 & n.39.

371 See *supra* note 108.

372 17 C.F.R. § 240.14e-1(a) (1990); see *supra* text following note 95; *supra* text ac-

4(f)(1)³⁷³ (in the case of issuer offers) establish a minimum offering period.³⁷⁴ These rules are designed to guard against the coercive effect that offers of short duration may have on shareholder decisionmaking.³⁷⁵ Second, rule 13e-4(f)(2)-(4) gives shareholders in issuer offers the same substantive protections that section 14(d) affords shareholders in third-party offers, namely the right to withdraw shares, to have shares purchased on a pro rata basis, and to receive the benefit of any increase in price.³⁷⁶ These substantive protections are intended to guard against the coercion engendered by offers that restrict the right of tendering shareholders to withdraw their shares or that permit shares to be purchased on a first-come, first-served basis, and to prevent bidders from unfairly discriminating among tendering shareholders. Third, rule 14d-8 modifies section 14(d)—which requires proration for ten calendar days in third party offers—by extending proration to the life of the offer.³⁷⁷ Aware that it lacked authority under section 14(d) to extend the statutory proration period, the SEC relied on its prophylactic rulemaking power under section 14(e) in adopting rule 14d-8.³⁷⁸ Therefore, rule 14d-8 prohibits

companying note 96.

373 17 C.F.R. § 240.13e-4(f)(1) (1990).

374 The minimum offering period for third-party offers has been 20 business days since the adoption of rule 14e-1 in 1979. In 1979, the SEC set the minimum offering period for issuer offers at 15 business days but several months later extended the period to 20 business days if the offer was in response to a third-party offer. Adoption of Amendments to Tender Offer Rules, Exchange Act Release No. 16,384, *supra* note 58, at 82,595. Then in 1986, the SEC extended the minimum offering period for all issuer offers to 20 business days. Adoption of Rules Amending Time Periods in Issuer Offers, Exchange Act Release No. 22,788, [1985-1986 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,954, at 87,974-75 (Jan. 14, 1986).

375 The requirements of rule 13e-4 and rule 14e-1 that the offeror must pay the consideration offered or return the tendered securities promptly after the termination or withdrawal of the offer, 17 C.F.R. §§ 240.13e-4(f)(5), 240.14e-1(c) (1990), are also examples of SEC measures designed to prevent unfair substantive conduct.

376 *Id.* § 240.13e-4(f)(2)-(4). Initially, the withdrawal and proration periods for issuer offers were both 10 business days. See Adoption of Rules Regarding Tender Offers by Issuers, Exchange Act Release No. 16,112, *supra* note 108, at 82,209. In 1986, the SEC extended the withdrawal period to 15 business days and the proration period to the life of the offer. Adoption of Rules Amending Time Periods in Issuer Offers, Exchange Act Release No. 22,788, *supra* note 374, at 87,975-77. Several months later the SEC extended the withdrawal period to the life of the offer. Adoption of All-Holders and Best-Price Rule, Exchange Act Release No. 23,421, *supra* note 83, at 83,196-97.

377 17 C.F.R. § 240.14d-8 (1990); see *supra* text accompanying note 84.

378 See *supra* note 84. The absence of express authority in § 14(d)(6) to extend the proration period caused two of the five Commissioners, including the Chairman, to conclude that the SEC also lacked authority under § 14(e). See Adoption of Pro Rata Rule, Exchange Act Release No. 19,336, *supra* note 84, at 85,652-54. Several commentators

first-come, first-served offers as a means of preventing the coercion and unfairness that such offers may entail. Finally, rule 14d-10³⁷⁹ (in the case of third-party offers) and rule 13e-4(f)(8)³⁸⁰ (in the case of issuer offers) are designed to prevent a bidder from discriminating against certain shareholders by excluding them from the offer or by offering and then paying them a lower price. These provisions, unlike the others discussed above, were adopted after *Schreiber*. Mindful of the absence of express rulemaking authority under section 14(d) and the limitation that *Schreiber* imposed on its rulemaking authority under section 14(e), the SEC adopted rule 14d-10 under section 14(d) and section 14(e).³⁸¹ In relying on both statutory provisions, the SEC was obviously hedging against the possibility that it lacked authority under one or the other of the provisions. Although section 14(d) does contain protections designed to ensure the fair and equal treatment of *tendering* shareholders, the SEC should not infer from these protections the authority to adopt a rule that ensures equality of treatment of *all* shareholders. Thus rule 14d-10 is best analyzed as if it had been adopted exclusively pursuant to the SEC's rulemaking authority under section 14(e). In adopting rule 13e-4(f)(8), the SEC did not have the option of relying on both section 14(d) and section 13(e) since section 14(d) does not apply to issuer offers.³⁸² Hence, rule 13e-4(f)(8) hinges on the SEC's rulemaking power under section 13(e).³⁸³ As prophylactic measures, rule 14d-10 and rule 13e-4(f)(8) ban discriminatory offers as a means of preventing unequal treatment of shareholders.

While the SEC's rules that shield against unfair tender offer practices may facilitate disclosure, they are not designed to pre-

have agreed with the dissenting Commissioners. They argue that the legislative history of § 14(d)(6) indicates that Congress did not intend to give the SEC rulemaking power to extend the proration period and that Congress did not change that intention when it amended § 14(e) in 1970. See Note, *supra* note 309; Note, *The Impact of Schreiber on the SEC Tender Offer Timing Rules*, 57 GEO. WASH. L. REV. 77 (1988); Recent Development, 36 VAND. L. REV. 1313 (1983).

379 17 C.F.R. § 240.14d-10 (1990); see *supra* text accompanying notes 86-88.

380 17 C.F.R. § 240.13e-4(f)(8) (1990).

381 See *supra* note 86.

382 See *supra* note 57.

383 In adopting rule 14d-10 and rule 13e-4(f)(8), the SEC also relied on § 23(a) of the Exchange Act, 15 U.S.C. § 78w(a) (1988). Section 23(a) authorizes the SEC to adopt rules "as may be necessary or appropriate to implement the provisions of [the Exchange Act]." The SEC's reliance on § 23(a), however, is misplaced because the all-holders and best-price requirements imposed by these rules are not implicit in § 14(d) or § 13(e). Cf. Filis, *supra* note 256, at 327-29 (contending that § 23(a) does not provide the SEC with sufficient authority to adopt an all-holders and best-price rule for issuer offers).

vent conduct that involves a failure to disclose or conduct that predictably gives rise to a failure to disclose.³⁸⁴ Instead, they are grounded on unconventional theories of fraud and manipulation—theories that the Court in *Schreiber* rejected. As a consequence, these rules are at risk of being invalidated by a court.³⁸⁵

IV. THE CONSTITUTIONALITY OF STATE TAKEOVER STATUTES

A. State Takeover Legislation Before CTS

Despite the extreme care that Congress took when it drafted the Williams Act to avoid tipping the scales in favor of either the offeror or the target company, the balance has nonetheless been upset on the state level by the enactment of an increasing number of state takeover statutes. The first such statute was enacted in Virginia four months before the passage of the Williams Act,³⁸⁶ and by the end of the 1970s thirty-seven states had passed takeover statutes as part of their blue sky laws.³⁸⁷ These first-generation statutes, as they came to be called, differed considerably as to the jurisdictional basis that was required for the statute to apply. For example, some based jurisdiction on the target's incorporation in the state or on location of the target's principal place of business in the state; others asserted jurisdiction if a specified percentage of target shareholders were residents of

384 The Court in *Schreiber* acknowledged that the 1970 amendment to § 14(e) gave the SEC the authority to regulate *nondeceptive* activities as long as the regulation was "reasonably designed" to prevent a failure to disclose. *Schreiber*, 472 U.S. at 11 n.11 (1985). The SEC's rules that shield against unfair tender offer practices do not satisfy the Court's test. They regulate nondeceptive activities as a "reasonably designed" means of preventing unfair substantive conduct but do not regulate practices involving misrepresentation or nondisclosure.

385 After the Court rendered its decision in *Schreiber*, legal commentators began to recognize that the SEC's rules guarding against unfair tender offer practices may be invalid. See 1 HAZEN, *supra* note 56, § 11.15, at 719 (rule 14e-1); Filfil, *supra* note 256, at 322-29 (rule 13e-4(f)(8) before it was adopted); Note, *supra* note 309, at 917-19 (rules 14d-3 and 14e-1). Congress has also expressed concern. See *Corporate Takeovers (Part 2): Hearings Before the Subcomm. on Telecommunications, Consumer Protection, and Finance of the House Comm. on Energy and Commerce*, 99th Cong., 1st Sess. 404-07 (1985). Recently, a three-judge panel of the Court of Appeals for the Second Circuit reversed a defendant's conviction for violation of rule 14e-3, 17 C.F.R. § 240.14e-3 (1990) (*see supra* note 100) in *United States v. Chestman*, 903 F.2d 75 (2d Cir.), *aff'd on rehearing*, No. 89-1276, 1990 US App LEXIS 18175 (2d Cir. 1990) (LEXIS, Genfed library, US App file) (en banc). One judge concluded, in reliance on *Schreiber*, that rule 14e-3 was invalid because it sought to prevent nondeceptive conduct. *Id.* at 84 (Mahoney, J.).

386 See *supra* note 38.

387 See Sargent, *On the Validity of State Takeover Regulation: State Responses to MITE and Kidwell*, 42 OHIO ST. L.J. 689, 690 n.7 (1981) (citing statutory provisions).

the state or if residents of the state held a specified percentage of target shares; and many of the statutes contained alternative bases for asserting jurisdiction.³⁸⁸ As a result, a bidder often had to comply with the laws of several states.³⁸⁹

Although the disclosure and substantive requirements of the state takeover statutes varied somewhat,³⁹⁰ the statutes all had the same objective: protecting target management and local industry from unwanted takeover attempts.³⁹¹ The statutes usually followed the federal regulatory model: they mandated disclosures regarding the offer and accorded target shareholders withdrawal, proration, and increased-price rights.³⁹² The statutes, however, generally went further than the federal provisions and required a waiting period of ten, twenty, or thirty days between the filing of the offer and the date on which the offer could commence.³⁹³ In addition, some of the statutes departed from the federal statute by permitting the state securities administrator to hold hearings and pass on the substantive fairness of the offer.³⁹⁴ The delay created by the precommencement waiting period and the hearing provisions afforded target management greater protec-

388 See ARANOW, EINHORN & BERLSTEIN, *supra* note 139, at 207-08; R. JENNINGS & H. MARSH, *supra* note 78, at 713.

389 See ARANOW, EINHORN & BERLSTEIN, *supra* note 139, at 208, 246 n.8 ("[A] tender offer for . . . securities of an Ohio corporation that had its principal place of business in Wisconsin, and a substantial portion of its assets in both Wisconsin and Indiana, would be subject to regulation under . . . the tender offer statutes of Ohio, Wisconsin, and Indiana.").

390 One commentator who studied the first-generation statutes suggested that "[s]tate takeover acts are similar to snowflakes—if you think you have found identical ones, you are probably not looking closely enough." Note, 7 J. CORP. L. 603, 603 (1982) (footnote omitted).

391 See L. LOSS, *supra* note 3, at 533; E. ARANOW & H. EINHORN, *supra* note 3, at 153 (stating that the impetus for the first-generation statutes was "[f]ears that established local concerns might be taken over by outside interests which in turn would close down plants and leave local residents jobless"); Langevoort, *State Tender-Offer Legislation: Interests, Effects, and Political Competency*, 62 CORNELL L. REV. 213, 238-40 (1977) (arguing that although the first-generation statutes purported to protect investors, they were really designed to serve the interests of entrenched incumbent management). The first-generation statutes usually contained exemptions for offers supported by target management and tender offers made by the target company for its own shares. See 1 T. HAZEN, *supra* note 56, § 11.21, at 761.

392 See ARANOW, EINHORN & BERLSTEIN, *supra* note 139, at 210-17.

393 See 1 T. HAZEN, *supra* note 56, § 11.21, at 760. The first-generation statutes prohibited the offeror, but not target management, from communicating with the target shareholders during the waiting period. See also ARANOW, EINHORN, & BERLSTEIN, *supra* note 139, at 218.

394 See ARANOW, EINHORN & BERLSTEIN, *supra* note 139, at 215-16.

tion than the federal statute, since it gave management more time to arrange defensive measures.³⁹⁵

No evidence in the legislative history indicates that Congress was aware of state tender offer legislation when it enacted the Williams Act,³⁹⁶ and thus Congress did not anticipate the veritable flood of state statutes that was to follow. Nonetheless, Congress provided for this eventuality, although perhaps unwittingly. By incorporating the Williams Act into the Exchange Act, Congress made the "savings clause" of the Exchange Act, section 28(a),³⁹⁷ applicable to the new federal tender offer statute and, therefore, preserved the rights and remedies of existing state law and left room for state regulation as long as it did not conflict with the federal provisions.

Because the state takeover legislation posed serious obstacles to the consummation of an unfriendly offer, hostile bidders routinely sought to enjoin state officials from enforcing the statutes. The bidders argued that the statutes were unconstitutional under the commerce and supremacy clauses of the United States Constitution. For the most part, these constitutional challenges were successful, and the courts ruled that the state takeover legislation both interfered impermissibly with interstate commerce and was preempted by the Williams Act.³⁹⁸

In their struggles to avoid the strictures of the state statutes, bidders usually found themselves closely aligned with the SEC, which consistently objected to the statutes on constitutional grounds also. The SEC contended that the state takeover statutes had resulted in an inconsistent, overlapping pattern of regulation

395 See *id.* at 217-19; Langevoort, *supra* note 391, at 238.

396 *Edgar v. MITE Corp.*, 457 U.S. 624, 631 n.6 (plurality opinion). Also, Congress was not aware of state tender offer legislation when it amended the Williams Act in 1970. Adoption of Amendments to Tender Offer Rules, Exchange Act Release No. 16,384, *supra* note 58, at 82,583 n.14.

397 15 U.S.C. § 78bb(a) (1988). Section 28(a), in pertinent part, states that "[t]he rights and remedies [of the Exchange Act] shall be in addition to any and all other rights and remedies that may exist at law or in equity" and that the provisions of the Exchange Act shall not affect "the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of [the Exchange Act or SEC rules adopted thereunder]." See *MITE*, 457 U.S. at 631 (plurality opinion) ("Congress did not explicitly prohibit States from regulating takeovers; it left the determination whether [a state statute] conflicts with the Williams Act to the courts.").

398 The bellwether was *Great W. United Corp. v. Kidwell*, 577 F.2d 1256 (5th Cir. 1978), *rev'd on other grounds sub nom. Leroy v. Great W. United Corp.*, 443 U.S. 173 (1979) (Idaho statute). With a few exceptions, the subsequent decisions followed *Kidwell*. See *Sargent*, *supra* note 387, at 629 & nn.17-20 (citing cases).

and had tipped the balance of regulation in favor of target companies.³⁹⁹ To buttress its preemption argument, the SEC adopted rule 14d-2(b)⁴⁰⁰ in 1979, which created a direct conflict between the federal regulatory scheme and most of the state statutes.⁴⁰¹ In contrast to the state legislation, which *prohibited* the commencement of an offer for at least ten days after public announcement, rule 14d-2(b) *required* commencement within five days.⁴⁰²

In 1982, in *Edgar v. MITE Corp.*,⁴⁰³ the Supreme Court was called upon to rule on the constitutionality of Illinois' first-generation takeover statute. The Court found the statute to be invalid, but since six opinions were filed in the case,⁴⁰⁴ the decision was less than definitive. Three Justices thought the case was moot,⁴⁰⁵ and the remaining six Justices disagreed on the proper resolution of the constitutional issues involved. The majority opinion, which mustered five votes, held that the Illinois statute was unconstitutional under the commerce clause because the burden the statute imposed on interstate commerce through *indirect* regulation was excessive in relation to the local putative benefits.⁴⁰⁶ The majority pointed out that the statute governed tender offers for target companies that were neither domiciliaries nor residents of Illinois.⁴⁰⁷ Four Justices, troubled that the statute applied even if none of the target shareholders were residents of Illinois, asserted that the statute violated the commerce clause because it *directly*

399 See, e.g., Brief for the SEC as Amicus Curiae at 15-62, *Leroy v. Great W. United Corp.*, 443 U.S. 173 (1979) (No. 78-759); Adoption of Amendments to Tender Offer Rules, Exchange Act Release No. 16,384, *supra* note 58, at 82,596.

400 17 C.F.R. § 240.14d-2(b) (1990).

401 See Adoption of Amendments to Tender Offer Rules, Exchange Act Release No. 16,384, *supra* note 58, at 82,583-84 ("[T]he conflict between Rule 14d-2(b) and [the] state statutes is so direct and substantial as to make it impossible to comply with both sets of requirements as they presently exist."); see also *supra* note 68.

402 The SEC's plan worked. Decisions rendered after the adoption of rule 14d-2(b) struck down state legislation under the supremacy clause on the ground that there was a direct conflict between the Williams Act and the state legislation. See Sargent, *supra* note 387, at 696-97 (citing cases).

403 457 U.S. 624 (1982).

404 Justices White, Powell, Stevens, O'Connor, Marshall, and Rehnquist filed opinions.

405 See *MITE*, 457 U.S. at 655-64 (Marshall, J., joined by Brennan, J., dissenting); *id.* at 664-67 (Rehnquist, J., dissenting). Justice Powell also thought the case was moot but joined in the majority opinion in view of the decision of five Justices to reach the merits. See *id.* at 646 (Powell, J., concurring in part).

406 See *id.* at 643-46 (opinion of White, J., joined by Burger, C.J., Powell, Stevens & O'Connor, JJ.).

407 See *id.* at 645.

regulated interstate commerce.⁴⁰⁸ Finally, three out of five Justices voting on the preemption issue concluded that the statute conflicted with the Williams Act and thus was void under the supremacy clause.⁴⁰⁹

Since it cannot be assumed that the four Justices who did not express their views on the preemption issue in *MITE* necessarily disagreed with the views of the plurality, the plurality preemption opinion is worth recounting. After pointing out that the SEC's preemptive provision, rule 14d-2(b), was not effective at the time of the tender offer involved in *MITE*, the plurality indicated that the resolution of the preemption issue turned on whether the Illinois statute frustrated the *purposes* of the Williams Act in some substantial way.⁴¹⁰ Instead of accepting the conclusion in *Piper* that investor protection was the sole purpose of the Act, the plurality reexamined the legislative history of the Act and subtly eroded *Piper's* analysis by stating: "There is no question that . . . Congress intended to protect investors. But it is also crystal clear that a major aspect of the effort to protect the investor was to avoid favoring either management or the takeover bidder."⁴¹¹

The opinion also recalled that Congress, in striving to attain a neutral balance, both rejected a precommencement notification provision and emphasized the importance of preventing target companies from delaying the tender offer process.⁴¹² The plurality then identified several provisions of the Illinois statute that upset the careful balance struck by Congress and thus tended to frustrate the purposes of the federal statute. The opinion first discussed the provisions of the Illinois statute that required a twenty-day precommencement waiting period and that allowed a state official to call a hearing. The plurality maintained that these provisions upset the balance by giving target management additional

408 See *id.* at 641-43 (White, J., joined by Burger, C.J., Stevens & O'Connor, JJ.).

409 See *id.* at 630-40 (White, J., joined by Burger, C.J. & Blackmun, J.). Two Justices disagreed with Justice White's preemption opinion. See *id.* at 646-47 (Powell, J., concurring in part); *id.* at 655 (Stevens, J., concurring in part and concurring in the judgment). Four Justices did not address the preemption issue. See *id.* at 655 (O'Connor, J., concurring in part); *id.* at 664 (Marshall, J., joined by Brennan, J., dissenting); *id.* at 667 (Rehnquist, J., dissenting).

410 *Id.* at 632.

411 *Id.* at 633 (citations omitted). Given the emphasis that Justice White gave to neutrality, it is somewhat surprising that Chief Justice Burger joined his opinion, for Chief Justice Burger had downplayed the significance of neutrality in *Piper*. See *supra* text accompanying notes 64-66.

412 *MITE*, 457 U.S. at 635-39.

time to combat the offer.⁴¹³ The opinion next turned to the provisions of the Illinois law that permitted a state official to prohibit an offer from going forward if the official found the offer to be inequitable. The plurality also found these provisions at odds with Congress' goals. Congress sought to preserve a neutral balance, the plurality argued, so that target shareholders would be free to make their own investment decisions.⁴¹⁴

Reading *MITE* broadly, the courts struck down virtually every first-generation takeover statute that came before them. Some of the statutes were thrown out on commerce clause grounds, others fell under the *MITE* plurality's supremacy clause argument, and a few were invalidated under both clauses.⁴¹⁵ But *MITE* did not mark the demise of state takeover regulation, for in the five-year period after the decision in *MITE* almost half of the states devised new takeover statutes. And although these second-generation statutes still sought to deter hostile offers for local companies, they were drafted with the intention of avoiding the constitutional defects of the first-generation statutes. First, the second-generation statutes were enacted as part of the states corporation codes so they applied only to domestic corporations. Second, instead of regulating the tender offer process itself, the statutes regulated

413 *Id.* at 634-39.

414 *Id.* at 639-40. Justice Powell, who disagreed with the plurality preemption opinion, stated: "[T]he Williams Act's neutrality policy does not necessarily imply a congressional intent to prohibit state legislation designed to assure—at least in some circumstances—greater protection to interests that include but often are broader than those of incumbent management." *Id.* at 646-47 (Powell, J., concurring in part). Justice Stevens, who also disagreed with the plurality preemption opinion, agreed with Justice Powell on the preemption issue and stated: "I am not persuaded . . . that Congress' decision to follow a policy of neutrality in its own legislation is tantamount to a federal prohibition against state legislation designed to provide special protection for incumbent management." *Id.* at 655 (Stevens, J., concurring in part and concurring in the judgment).

415 See *L.P. Acquisition Co. v. Tyson*, 772 F.2d 201 (6th Cir. 1985) (Michigan statute); *Mesa Petroleum Co. v. Cities Serv. Co.*, 715 F.2d 1425 (10th Cir. 1983) (Oklahoma statute); *Televest, Inc. v. Bradshaw*, 697 F.2d 576 (4th Cir. 1983) (Virginia statute); *Martin Marietta Corp. v. Bendix Corp.*, 690 F.2d 558 (6th Cir. 1982) (Michigan statute); *National City Lines v. LLC Corp.*, 687 F.2d 1122 (8th Cir. 1982) (Missouri statute); *Newell v. Connolly*, 624 F. Supp. 126 (D. Mass. 1985) (Massachusetts statute); *Esmark, Inc. v. Strode*, 639 S.W.2d 768 (Ky. 1982) (Kentucky statute); *Sharon Steel Corp. v. Whaland*, 124 N.H. 1, 466 A.2d 919 (1983) (New Hampshire statute). *But see* *Cardiff Acquisitions v. Hatch*, 751 F.2d 906 (8th Cir. 1984) (revised first-generation Minnesota statute held constitutional); *Agency Rent-A-Car, Inc. v. Connolly*, 686 F.2d 1029 (1st Cir. 1982) (Massachusetts statute not preempted by the Williams Act, and case remanded for consideration of commerce clause issue). For a discussion of these cases, see Warren, *Developments in State Takeover Regulation: MITE and Its Aftermath*, 40 BUS. LAW. 671, 686-94 (1985).

the internal affairs of target companies after the tender offer was completed.⁴¹⁶

In the post-MITE era, four major types of second-generation statutes emerged—control share acquisition statutes, fair price statutes, cash-out statutes, and business combination statutes—and some states adopted more than one kind.⁴¹⁷

Control share acquisition statutes provide that the acquisition of a control block of voting shares in a target company must be approved by a majority of the disinterested shareholders.⁴¹⁸ A few of these statutes require approval of the acquisition itself, whereas all the others require approval of the right to vote the shares acquired.⁴¹⁹ Fair price statutes typically provide that a successful bidder, who subsequently wants to effect a second-step "business combination" with the target, must obtain supermajority approval from the disinterested shareholders (as well as all shareholders) unless (1) the combination is approved by the target's board before the bidder obtains control, or (2) the bidder pays a "fair price" to those nontendering shareholders who are forced into the second-step combination.⁴²⁰ Cash-out statutes require a bidder who acquires a controlling interest in a target company (whether or not the bidder intends a second-step acquisition) to

416 For a discussion of the second-generation takeover statutes, see generally Block, Barton & Roth, *State Takeover Statutes: The "Second Generation"*, 13 SEC. REG. L.J. 332 (1986); Hazen, *State Anti-Takeover Legislation: The Second and Third Generations*, 23 WAKE FOREST L. REV. 77 (1988); Pinto, *Takeover Statutes: The Dormant Commerce Clause and State Corporate Law*, 41 U. MIAMI L. REV. 425 (1987); Profusek & Gompf, *State Takeover Legislation After MITE: Standing Pat, Blue Sky, or Corporation Law Concepts?*, 7 CORP. L. REV. 3 (1983); Sargent, *Do the Second-Generation State Takeover Statutes Violate the Commerce Clause?*, 8 CORP. L. REV. 3 (1985).

417 See 3 R. WINTER, R. ROSENBAUM, M. STUMPF & L. PARKER, *SHARK REPELLENTS AND GOLDEN PARACHUTES: A HANDBOOK FOR THE PRACTITIONER (STATE TAKEOVER STATUTES AND POISON PILLS)* § 1.1, at 4-5; § 1.2, at 7-12 (Supp. 1989) [hereinafter WINTER, ROSENBAUM, STUMPF & PARKER] (citing statutory provisions and effective dates). Most of the second-generation statutes either (1) permit a corporation to opt out of the statute's provisions by an amendment to the articles of incorporation or bylaws or by a specified vote of the board of directors or (2) require the corporation to elect to be covered by the statute through a comparable process.

418 Ohio was the first state to adopt a control share acquisition statute, doing so less than six months after the decision in *MITE*. For a discussion of the Ohio statute, see Raup, *Has Ohio Avoided the Wake of MITE? An Analysis of the Constitutionality of the Ohio Control Share Acquisition Act*, 46 OHIO ST. L. J. 203 (1985).

419 See 3 WINTER, ROSENBAUM, STUMPF & PARKER, *supra* note 417, § 2, at 15-26.5 (Supp. 1989). The control share acquisition statutes in Ohio and Hawaii are the only ones that require shareholder approval of the acquisition itself. *Id.* at 19.

420 See *id.* § 4, at 41-49. Maryland was the first state to pass a fair price statute. For a discussion of the Maryland statute, which was adopted in 1983, see Note, *Second Generation State Takeover Legislation: Maryland Takes a New Tack*, 83 MICH. L. REV. 433 (1984).

pay a "fair value" to those nontendering shareholders who request to be bought out.⁴²¹ Business combination statutes prohibit a bidder who obtains a controlling interest in a target company from engaging in a "business combination" with the target for a two-to-five year period unless the target's board approves the combination before the bidder acquires control. Further, at the end of this moratorium, the bidder may engage in the combination only with the consent of a majority (or supermajority) of disinterested shareholders or in some states upon paying all shareholders a "fair price."⁴²²

Initially, it appeared as if the second round of state takeover legislation was as unconstitutional as the first round. Control share acquisition statutes—the only ones challenged—were consistently struck down under the commerce clause or the supremacy clause or under both clauses, and the rhetoric of lower federal court decisions suggested that the other three types of second-generation statutes would also fail to survive constitutional scrutiny if an attack were mounted.⁴²³ In 1987, the Supreme Court heard one of these cases on appeal; the case was *CTS Corp. v. Dynamics Corp. of America*.⁴²⁴

421 See 3 WINTER, ROSENBAUM, STUMPF & PARKER, *supra* note 417, § 5, at 51-54 (Supp. 1989). Pennsylvania was the first state to adopt a cash-out law. For a discussion of the Pennsylvania statute, which was enacted in 1983, see Newlin & Gilmer, *The Pennsylvania Shareholder Protection Act: A New State Approach to Deflecting Corporate Takeover Bids*, 40 BUS. LAW. 111 (1984).

422 See 3 WINTER, ROSENBAUM, STUMPF & PARKER, *supra* note 417, § 3.1-2, at 28-40.7 (Supp. 1989). New York was the first state to adopt a business combination statute. For a discussion of the New York statute, which was passed in 1985, see Miles, *The Constitutionality of State Business Combination Legislation: New York's Section 912*, 8 CARDOZO L. REV. 1025 (1987).

423 See *Fleet Aerospace Corp. v. Holderman*, 796 F.2d 135 (6th Cir. 1986), *vacated and remanded sub nom. Ohio v. Fleet Aerospace Co.*, 481 U.S. 1026 (1987) (Ohio statute); *Dynamics Corp. of Am. v. CTS Corp.*, 794 F.2d 250 (7th Cir. 1986), *rev'd*, 481 U.S. 69 (1987) (Indiana statute); *Gelco Corp. v. Coniston Partners*, 652 F. Supp. 829 (D. Minn. 1986) (Minnesota statute); *Terry v. Yamashita*, 643 F. Supp. 161 (D. Hawaii 1986) (Hawaii statute); *APL Limited Partnership v. Van Dusen Air, Inc.*, 622 F. Supp. 1216 (D. Minn. 1985) (Minnesota statute); *Icahn v. Blunt*, 612 F. Supp. 1400 (W.D. Mo. 1985) (Missouri statute).

424 481 U.S. 69 (1987). By the time of the Supreme Court's decision in *CTS*, 21 states had adopted one or more takeover statutes that had taken effect: Hawaii, Indiana, Minnesota, Missouri, Ohio (control share acquisition statutes); Connecticut, Georgia, Illinois, Kentucky, Louisiana, Maryland, Michigan, Mississippi, Pennsylvania, Virginia, Washington, Wisconsin (fair price statutes); Maine, Pennsylvania, Utah (cash-out statutes); Indiana, Kentucky, Missouri, New Jersey, New York (business combination statute). See 3 WINTER, ROSENBAUM, STUMPF & PARKER, *supra* note 417, § 1.2, at 7-11 (1988) (citing statutory provisions and effective dates).

B. *The CTS Case*

1. Denial of Individual Autonomy to Target Shareholders

CTS, the Supreme Court's third visit to the tender offer provisions of the Williams Act, involved the application of Indiana's control share acquisition statute⁴²⁵ to the efforts of Dynamics Corporation of America (Dynamics) to acquire a controlling interest in CTS Corporation (CTS), an Indiana corporation.⁴²⁶ At a time when it owned 9.6% of the common stock of CTS, Dynamics initiated a cash tender offer for additional CTS common shares. This offer, if successful, would have brought Dynamics' ownership interest in CTS to 27.5%. Several days before Dynamics commenced its offer, Indiana adopted a control share acquisition statute, which applied to all "issuing public corporations." The statute defined an "issuing public corporation" as every Indiana corporation that had a substantial presence in Indiana and a substantial number of Indiana shareholders.⁴²⁷ For a transition period of approximately seventeen months, the board of directors of such a corporation could opt into the provisions of the statute.⁴²⁸ Thereafter, the statute automatically applied unless the company amended its articles of incorporation or bylaws to opt out.⁴²⁹ Before Dynamics' tender offer expired, the board of CTS, an "issuing public corporation," opted into the statute.

Under the Indiana statute, shares acquired in an "issuing public corporation" that bring the acquiror to or above one of three threshold levels of voting power (one-fifth, one-third, or one-half) are called "control shares." And the statute strips all "control shares" of voting rights unless a majority of the target shareholders (excluding the acquiror and target management) agree to restore the voting power.⁴³⁰ The shareholders vote on

425 IND. CODE ANN. §§ 23-1-42-1 to -11 (West Supp. 1990).

426 A summary of Dynamics' attempted takeover of CTS is set forth in *CTS*, 481 U.S. at 75.

427 IND. CODE ANN. § 23-1-42-4(a) (West Supp. 1990) (defining an "issuing public corporation" as an Indiana corporation that has (1) 100 or more shareholders, (2) its principal place of business, its principal office or substantial assets within Indiana, and (3) either more than 10% of its shareholders resident in Indiana, more than 10% of its shares owned by Indiana residents, or 10,000 shareholders resident in Indiana).

428 *Id.* § 23-1-17-3(b).

429 *Id.* § 23-1-42-5.

430 *Id.* §§ 23-1-42-1, -3, -5, -9. Thus, only the 17.9% of CTS' common shares that Dynamics sought in the tender offer were "control shares" whose voting power would be determined by a vote of CTS' disinterested shareholders. *See id.* § 23-1-42-1 comment.

this matter at their next annual meeting or at a special meeting called at the request of a person who proposes to make or has made a "control share acquisition."⁴³¹ Once such a request is made, target management must schedule the special meeting within fifty calendar days.⁴³² Hence, a bidder who wants an early resolution of the issue will presumably request a special meeting on the commencement date of the offer.⁴³³ If the shareholders decline to restore voting rights to the "control shares," the target may redeem the shares at their fair market value, but it is not obligated to do so.⁴³⁴

Seeking to prevent its shares from being sterilized once it crossed the twenty percent threshold of voting power, Dynamics sued to enjoin CTS' use of the statute. The district court granted the requested injunctive relief and entered an order declaring that the Indiana statute was preempted by the Williams Act and impermissibly burdened interstate commerce.⁴³⁵ The Court of Appeals for the Seventh Circuit affirmed the judgment of the district court.⁴³⁶ The Supreme Court noted probable jurisdiction for an appeal⁴³⁷ and voted 6-3 to reverse the Seventh Circuit's decision. Writing for the Court, Justice Powell held that the Indiana statute was not preempted by the Williams Act and did not violate the commerce clause.⁴³⁸

431 *Id.* §§ 23-1-42-7, -9.

432 *Id.* § 23-1-42-7(b). The offeror must agree to pay for the expenses of the special meeting. *Id.* § 23-1-42-7(a).

433 *See* CTS, 481 U.S. at 70 n.2. The Court made two observations about the statute to demonstrate that tendering shareholders will usually be able to vote their shares at the special meeting even though they may not be the owners of the shares on the date of the meeting. First, if the bidder requests a special meeting on the commencement date of the offer, target management is most likely obligated to set the record date and send the notice of the meeting during the first 20 business days of the offer. Second, since tendered shares cannot be purchased under federal law until 20 business days after the offer commences, the record date will be set before the offeror can purchase any shares. *Id.*

434 IND. CODE ANN. § 23-1-42-10(b) (West Supp. 1990).

435 Dynamics Corp. of Am. v. CTS Corp., 637 F. Supp. 389 (N.D. Ill.), *aff'd*, 794 F.2d 250 (7th Cir. 1986), *rev'd*, 481 U.S. 69 (1987).

436 Dynamics Corp. of Am. v. CTS Corp., 794 F.2d 250 (7th Cir. 1986), *rev'd*, 481 U.S. 69 (1979).

437 CTS Corp. v. Dynamics Corp. of Am., 479 U.S. 810, *noting prob. juris. in* 794 F.2d 250 (7th Cir. 1986).

438 Justice Powell was joined by Chief Justice Rehnquist and Justices Brennan, Marshall, and O'Connor. Justice Scalia concurred in a separate opinion. Justice White filed a dissenting opinion regarding both the commerce clause and preemption issues. He was joined in his commerce clause reasoning by Justices Blackmun and Stevens.

The Court began its opinion with an analysis of the preemption issue and reasoned that since compliance with both the Williams Act and the Indiana statute was possible, a preemptive conflict existed only if the state statute frustrated the purposes of the federal statute.⁴³⁹ The Court maintained that investor protection was the primary purpose of the Williams Act and that the Indiana statute advanced, not hampered, this purpose. The Court believed that the Indiana statute was designed to protect target shareholders from the coercive aspects of some tender offers by allowing target shareholders to act collectively. Citing the SEC's study of two-tier tender offer pricing,⁴⁴⁰ the Court explained that target shareholders often tender their shares—even when they think that the offer is not in the best interests of the target company—to guard against the possibility that they will be forced to sell their shares at a lower price in a second-step transaction.⁴⁴¹

The Court indicated that it was not bound by the plurality view in *MITE* that neutrality was a purpose of the Williams Act, since this view was not accepted by a majority of the Court. Nonetheless, the Court opined that even under this broad interpretation of the purposes of the Act, the Indiana statute passed constitutional muster because (unlike the Illinois statute considered in *MITE*) it did not favor target management over offerors.⁴⁴² First, the Court asserted that the Indiana statute did not impose an absolute delay in consummating tender offers. The Court argued that the Indiana statute neither required a bidder to keep its offer open beyond the minimum twenty-business-day offering period prescribed by federal law nor prevented a bidder from purchasing tendered shares immediately after the close of the offer.⁴⁴³

Second, the Court contended that if offerors feared an adverse shareholder vote regarding the enfranchisement of the tendered "control shares," they could condition their obligation to

439 *CTS*, 481 U.S. at 78-79. In his concurring opinion, Justice Scalia argued that a state statute may be preempted by the Williams Act on the basis of a conflicting "provision" but not on the basis of a conflicting "purpose." *Id.* at 96 (Scalia, J., concurring in part and in the judgment).

440 Notice of Possible Action Regarding Two-Tier Tender Offer Pricing and Non-Tender Offer Purchase Programs, Exchange Act Release No. 21,079, *supra* note 344.

441 *CTS*, 481 U.S. at 82-84. In dissent, Justice White argued that the Indiana statute, which protected target shareholders as a group, was inconsistent with the Williams Act, which protected target shareholders as individuals. *Id.* at 97-99 (White, J., dissenting).

442 *Id.* at 81.

443 *Id.* at 83-84.

purchase these shares on voting rights being conferred within a certain time period. Admitting that some delay would be introduced into the tender process if a bidder made its offer conditional, the Court asserted that this delay was not unreasonable. In support of its assertion, the Court noted that a provision in section 14(d) of the Williams Act granted target shareholders the right to withdraw unpurchased shares after sixty calendar days from the commencement of the offer. The Court construed this provision as evidence that Congress considered sixty calendar days to be the maximum offering period. Based on this interpretation, the Court argued that the federal timetable for tender offers was actually longer than the one envisioned by the Indiana statute, which ensured that it was possible for the shareholder vote to occur within fifty calendar days following the commencement of the offer.⁴⁴⁴

Finally, the Court maintained that invalidating the Indiana statute on the grounds that it might introduce some delay into the tender offer process would be tantamount to invalidating a number of other state corporation laws of unquestioned validity. As examples, the Court mentioned state statutes authorizing staggered terms for directors and cumulative voting, both of which delay an offeror's ability to gain control of the board of directors.⁴⁴⁵

Next, the Court turned to an analysis of the commerce clause issue and offered two threshold reasons why the Indiana statute survived dormant commerce clause scrutiny. First, the statute did not discriminate against interstate commerce because it applied equally to both local and out-of-state offerors.⁴⁴⁶ And second, the statute did not burden interstate commerce by creating an impermissible risk of inconsistent regulation by different states, since it applied only to target companies incorporated in Indiana.⁴⁴⁷

The Court never explicitly evaluated the indirect effects of the Indiana statute on interstate commerce.⁴⁴⁸ Instead of balanc-

444 *Id.* at 84-85.

445 *Id.* at 85-86.

446 *Id.* at 87-88.

447 *Id.* at 88-89. In dissent, Justice White argued that the Indiana statute "directly regulat[ed]" the purchase and sale of shares of stock in interstate commerce and was therefore unconstitutional. *Id.* at 99-101 (White, J., dissenting).

448 In his concurring opinion, Justice Scalia argued that such an evaluation was unnecessary, since a conclusion that the Indiana statute neither discriminated against interstate commerce nor created an impermissible risk of inconsistent regulation by different

ing the putative local benefits of the state legislation against the incidental burdens the legislation imposed on interstate commerce, as it had done in *MITE*, the Court asserted that a state that creates a corporation is justified in enacting a law that defines the attributes of the corporation's shares and that protects the corporation's shareholders, even if that law affects certain aspects of interstate commerce.⁴⁴⁹ The Court therefore concluded that even if the Indiana statute "decrease[d] the number of successful tender offers for Indiana corporations, this would not offend the [c]ommerce [c]lause."⁴⁵⁰

2. An Analysis of *CTS*

The Supreme Court's ruling in *CTS* was not generally anticipated by bench or bar,⁴⁵¹ but in light of the Court's earlier Williams Act opinions, the *CTS* ruling was not surprising. In *Piper* and *Schreiber*, the Court had already sapped the Williams Act of much of its remedial and substantive content by deferring to state common law. It would have been odd, therefore, if the Court in *CTS* had checkmated the states' legislative efforts at tender offer regulation in deference to an exclusive right of the federal government to regulate takeovers under the supremacy or commerce clause. Nonetheless, the Court in *CTS* took a giant step forward in strengthening the hand of target managers intent on resisting an unwanted takeover bid. *Piper* and *Schreiber* had not countenanced the defensive measures of target companies. Rather, these two opinions had given the states virtually undivided power to judge such measures. In contrast, by validating a state takeover statute, *CTS* directly sanctioned a standardized, ready-made defensive tactic, a tactic that may be largely immune from the type of

states was sufficient. *Id.* at 94-96 (Scalia, J., concurring in part and concurring in the judgment). Since *MITE*, the Court seems to be moving away from making a distinction between the "direct" and "indirect" effects that state regulation has on interstate commerce. *See, e.g.*, *Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 379 (1983); *cf. Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. 573, 578-79 (1986). Legal commentators disagree on how the dormant commerce clause should be applied, and four schools of thought have emerged. Only two of these schools of thought require a balancing of interests. *See Cox, The Constitutional "Dynamics" of the Internal Affairs Rule—A Comment on CTS Corporation*, 13 J. CORP. L. 317, 318 n.7 (1988).

449 *CTS*, 481 U.S. at 89-91.

450 *Id.* at 94.

451 *See Oesterle, Delaware's Takeover Statute: Of Chills, Pills, Standstills, and Who Gets Iced*, 13 DEL. J. CORP. L. 879, 933 (contending that "no one, nary a lower federal court nor a commentator, was even close to foreseeing the result in the *CTS* case").

state-law challenges that are usually made when target directors customize their own defensive measures.⁴⁵²

That the Indiana legislature intended its control share acquisition statute to function as a promanagement, antitakeover device seems fairly obvious. The State of Indiana itself, which intervened in the *CTS* litigation, conceded that the statute was designed in part to protect local economic interests,⁴⁵³ and, like other state takeover legislation, the Indiana statute accomplishes this objective by discouraging potential bidders from making tender offers for local companies or by hindering the successful completion of such offers. Despite this concession, the *CTS* Court chose to focus exclusively on the protection that the statute purported to provide target shareholders and refused to acknowledge that shareholder protection was simply a guise for the statute's true purpose: economic protectionism. The Court's failure (or unwillingness) to come to terms with the ulterior purpose and unavoidable effects of the statute rendered its analysis both disingenuous and unpersuasive. Indeed, as the discussion below argues, the Indiana statute should have been declared unconstitutional under both the supremacy clause and the commerce clause.

(a) *The Preemptive Force of the Williams Act.*—At its core, the preemption analysis in *CTS* rested on the Supreme Court's conclusion that the Indiana control share acquisition statute advanced the investor protection purpose of the Williams Act by addressing the collective action problem that coercive offers present. To be sure, in certain tender offers some target shareholders do tender

452 *But see* *Samjens Partners I v. Burlington Indus.*, 663 F. Supp. 614 (S.D.N.Y. 1987) (reviewing under state law a target board's decision to opt out of a control share acquisition statute for a friendly leveraged buyout—but not for a competing hostile offer—but holding that the decision was protected by the business judgment rule). On the relationship between state takeover statutes and privately adopted defensive measures, see Booth, *State Takeover Statutes Revisited*, 88 MICH. L. REV. 120, 121 (1989) [hereinafter *State Takeover Statutes Revisited*] (contending that a state's adoption of a takeover statute may be interpreted by the judiciary as "a condemnation of other nonstandardized tactics"); Booth, *The Promise of State Takeover Statutes*, 86 MICH. L. REV. 1635, 1692 (1988) (referring to the Indiana statute as a "statutory poison pill"); Cox, *supra* note 448, at 326 (indicating that the second-generation state statutes are patterned on privately adopted defensive tactics); Oesterle, *supra* note 451, at 885 (suggesting that the second-generation state statutes are not as lethal as privately adopted defensive tactics).

453 *See CTS*, 481 U.S. at 100-01 (White, J., dissenting); *see also* Butler, *State Takeover Legislation, the Market for Corporate Charters, and the Scope of Federal Intervention: A Comment on Hitzeman*, *Indiana's Control Share Acquisition Statute*, 27 AM. BUS. L.J. 291, 297 (1989) (pointing out that the Indiana statute was passed specifically to block the takeover of Arvin Industries, an Indiana corporation, by the Belzberg family of Canada).

their shares even though they believe that the price is inadequate. These shareholders are pressured into tendering because they know or anticipate that they will be bought out at an even lower price in a second-step transaction if the offer is successful. By enabling target shareholders to act collectively to reject such coercive offers, the Indiana statute, therefore, does protect investors. The measure of protection, however, is negligible in the aggregate. By the time the Indiana statute was passed, the number of two-tier and partial offers—where coercion is most likely to occur⁴⁵⁴—had declined dramatically, and such offers continue to represent a very small percentage of all tender offers.⁴⁵⁵ Two months after the Court handed down the *CTS* opinion, an SEC Commissioner, in congressional testimony regarding the issue of coercive tender offers, concluded that “the market appears to have corrected any problem that may have existed.”⁴⁵⁶ Given the waning frequency of two-tier and partial offers, protecting target shareholders from the coercive aspects of tender offers could hardly have been the purpose of the Indiana statute. Therefore, the Court’s reliance on this purpose as the linchpin of its pre-emption analysis was naive.

Even if the Indiana legislation could be construed as a bona fide attempt to protect target shareholders, the protection it provides conflicts with the investor protection that is implicit in the Williams Act. The Indiana statute protects shareholders as a group, whereas the Williams Act requires the disclosure of infor-

454 See Oesterle, *supra* note 451, at 900 n.89 (contending that two-tier and partial offers are the primary vehicles for the most coercive offers but noting that “even any-or-all tender offers have coercive potential”). *But cf.* Coffee, *The Uncertain Case for Takeover Reform: An Essay on Stockholders, Stakeholders and Bust-Ups*, 1988 WIS. L. REV. 435, 439 (contending that coercive tender offers are a “myth”); Fischel, *supra* note 53, at 63 (concluding that the alleged coercive effect of tender offers is not a problem).

455 See Johnson & Millon, *Missing the Point About State Takeover Statutes*, 87 MICH. L. REV. 846, 846-87 (1989); Langevoort, *The Supreme Court and the Politics of Corporate Takeovers: A Comment on CTS Corp. v. Dynamics Corp. of America*, 101 HARV. L. REV. 96, 105 (1987).

456 *Regulating Hostile Corporate Takeovers: Hearings on S. 227, S. 678, S. 1264, S. 1323 and S. 1324 Before the Senate Comm. on Banking, Housing, and Urban Affairs*, 100th Cong., 1st Sess. 97 (1987) (statement of Charles C. Cox, Commissioner of the SEC). Furthermore, the empirical SEC study that the *CTS* Court cited shows that the premiums offered in any-or-all tender offers are only slightly larger than the sum of the premiums offered in two-step transactions. See Notice of Possible Action Regarding Two-Tier Pricing and Non-Tender Offer Purchase Programs, Exchange Act Release No. 21,079, *supra* note 344, at 86,925. One commentator has suggested that the states’ adoption of takeover statutes may be responsible for the demise of coercive offers. See Booth, *State Takeover Statutes Revisited*, *supra* note 452, at 121.

mation so that individual target shareholders can make their own investment decisions.⁴⁵⁷ By providing collective shareholder protection at the expense of individual shareholder autonomy, the Indiana statute clashes with the federal statute and therefore falls within the prohibitions of the supremacy clause.

The Indiana statute is also preempted by the Williams Act because it upsets the neutral regulatory balance between the tender offeror and target management that was struck by Congress when it adopted the Williams Act. The delay that the Indiana statute builds into the tender offer process enhances target management's ability to defeat a tender offer—to the detriment of target shareholder welfare—and therefore tilts the regulatory balance in favor of target management. That the Indiana statute consistently serves as an engine of delay is readily apparent. No rational bidder that is governed by the Indiana statute will obligate itself to purchase tendered shares until voting rights have been restored to the shares. Accordingly, bidders will be forced to make their offers conditional, as the Court suggested they may, on the restoration of voting rights. Since the Indiana statute permits target management to delay shareholder consideration of the enfranchisement issue for up to fifty calendar days after the commencement of the offer, the practical impact of the statute is to preclude bidders from consummating their offers until the expiration of this fifty-calendar-day period. Thus, a bidder that has stipulated that its offer will be held open for the minimum twenty-business-day (twenty-eight-calendar-day) period required by federal law must wait an additional twenty-two calendar days before accepting tendered shares for payment.

The Court argued that this delay was not unreasonable because the Williams Act contemplates that shares will be accepted for payment during the time period starting with the expiration of the offer (when shareholder withdrawal rights terminate)⁴⁵⁸

457 See *supra* note 441. It has been suggested by several commentators that if target shareholders want protection from coercive bids, charter amendments either imposing control share voting restrictions or requiring that a fair price be paid in any second-step acquisition provide a less intrusive means of protection than state takeover statutes. See, e.g., Langevoort, *supra* note 455, at 105; Macey, *State Anti-Takeover Legislation and the National Economy*, 1988 WIS. L. REV. 467, 469 (1988). Target management, however, seldom pursues such charter amendments. See Fischel, *supra* note 53, at 66-67 ("It is possible that firms lobby for anti-takeover statutes in those situations where shareholders would refuse to approve a charter amendment with the same effect.")

458 The Court stated that a bidder cannot purchase shares until the offer expires. See *CTS*, 481 U.S. at 74 n.2. Actually, shares can be purchased as soon as withdrawal rights

and ending with the expiration of sixty calendar days after the commencement of the offer (when shareholder withdrawal rights are reinstated)—a period that may span thirty-two calendar days. The Court's reasoning is fallacious. Delay imposed by a state takeover statute is only unreasonable if it provides target management with more time to defeat an offer than does the federal statute. The regulatory scheme of the Williams Act is structured so that target management can act to stymie an offer only during the offering period—not during the post-offering period when bidders are required to purchase tendered shares—since once the offering period expires, target shareholder decisionmaking stops and efforts by target management to resist the offer would be unavailing. The Indiana statute compels bidders to make their offers contingent on the occurrence of a post-offering-period event over which target shareholders have collective control. Thus, the Indiana statute gives target management additional time to influence the decisionmaking of target shareholders and to block the offer.⁴⁵⁹ Therefore, the delay created by the Indiana statute constitutes a delay beyond what the Williams Act provides. As a consequence, it disrupts the neutral balance necessary for the intended operation of the Act.⁴⁶⁰

(b) *The Commerce Clause as an Independent Bar to State Takeover Legislation.*—The existence of a federal statute regulating interstate tender offers does not obviate the need to evaluate state takeover statutes under the commerce clause, and the resolution of the preemption issue is not determinative of the fate of a state statute attacked on commerce clause grounds.⁴⁶¹ Indeed, the courts view the commerce clause as an independent force that

terminate. Under the current regulatory scheme, the distinction is irrelevant since withdrawal rights exist for the life of the offer. Prior to 1986—when withdrawal rights did not exist for the life of the offer—the distinction did matter, and offerors were able to accept shares for payment at an earlier point in time than is permitted under current law. See 17 C.F.R. § 240.14d-7(a)(2) (1980).

459 See Note, *Second Generation State Takeover Statutes and Shareholder Wealth: An Empirical Study*, 97 YALE L.J. 1193, 1200 (1988).

460 See *supra* text accompanying note 445. The Court's analogy between the Indiana takeover statute and other state statutes that produce delays in control shifts is inappropriate. The Indiana statute creates delay in consummating the tender offer itself, whereas statutes authorizing staggered terms for directors or cumulative voting create delay in obtaining control of the board of directors once the tender offer has been completed.

461 Cf. Cox, *supra* note 468, at 337 n.116 (stating that "the presence of federal regulation within the subject matter the state purports to regulate may strengthen the commerce clause argument even when preemption would otherwise be inappropriate").

is capable of barring state takeover regulation notwithstanding the adoption of the Williams Act.⁴⁶² Furthermore, the courts routinely scrutinize state takeover statutes under the commerce clause even when they hold that the statute is preempted by the Williams Act. Of course, in this situation the commerce clause analysis is academic, since the statute is unenforceable by reason of the supremacy clause. Despite their independence, the preemption and commerce clause analyses of state takeover legislation frequently shade into each other at the edges, and the Court's evaluation of the Indiana statute in *CTS* is a prime example.⁴⁶³

The commerce clause gives Congress virtually unlimited power to regulate interstate commerce. Further, it possesses a dormant power to prohibit certain state regulation of interstate commerce, and gives Congress the power both to authorize state regulation that would otherwise violate the commerce clause and to prohibit state regulation that could otherwise be upheld under the commerce clause.⁴⁶⁴ Since the Williams Act does not alter what the dormant commerce clause prohibits or permits, the validity of state takeover legislation under the commerce clause, as the *CTS* Court recognized, turns on dormant commerce clause scrutiny.

According to traditional dormant commerce clause doctrine, state legislation that affects or regulates interstate commerce (such as the Indiana statute) is invalid if it poses a threat of inconsistent regulation of the same activity by different states or if it discriminates against out-of-state interests.⁴⁶⁵ The *CTS* Court was correct in concluding that the Indiana statute did not create a risk of multiple and inconsistent regulation of interstate tender offers. If each state followed the Indiana model and limited the reach of its takeover legislation to tender offers for companies incorporated in the state, no tender offer would be subject to the takeover statute of more than one state.

462 See *Dynamics Corp. of Am. v. CTS Corp.*, 794 F.2d 250, 263 (7th Cir. 1986), *rev'd on other grounds*, 481 U.S. 69 (1987).

463 See Oesterle, *supra* note 451, at 947 (observing that the preemption and commerce clause issues in *CTS* "merge to a substantial degree").

464 See L. TRIBE, *AMERICAN CONSTITUTIONAL LAW* § 6-27, at 497, § 6-33, at 524-27 (2d ed. 1987).

465 See Langevoort, *supra* note 455, at 100. *But see* Regan, *Siamese Essays: (I) CTS Corp. v. Dynamics Corp. of America and Dormant Commerce Clause Doctrine; (II) Extraterritorial State Legislation*, 85 MICH. L. REV. 1865, 1869 (1987) (contending that the issue of inconsistent regulation is really an issue of extraterritoriality, which does not implicate the commerce clause).

The Court's analysis of whether the Indiana statute was discriminatory vis-a-vis out-of-state parties, however, was deficient. The Court reasoned that because the Indiana statute applied equally to Indiana and out-of-state offerors, the statute would not have a discriminatory effect on interstate commerce. If the Court had been more robust in its analysis, it would have gone beyond the facial impartiality of the statute and recognized that the dormant commerce clause prohibits state statutes with a *discriminatory purpose*⁴⁶⁶ and that the economically protectionist purpose of the Indiana statute was discriminatory.⁴⁶⁷ The Indiana statute is designed to preserve employment for Indiana residents and supply contracts for Indiana companies by making the relocation of employment and assets outside Indiana more difficult. Therefore, the Indiana legislation favors Indiana workers and suppliers at the expense of non-Indianans who would become workers and suppliers if a successful bidder decided to move the target's operations to another state where they could be performed more efficiently.⁴⁶⁸ In sum, the economic protectionism of local interests that the Indiana statute fosters is precisely the type of discrimination that the dormant commerce clause was meant to prevent, and hence

466 See Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 MICH. L. REV. 1091, 1125-37 (1986) (arguing that dormant commerce clause scrutiny turns on whether the state statute has a discriminatory purpose).

467 The Supreme Court has consistently held that protectionist state regulation is constitutionally impermissible. See, e.g., *Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. 573, 579 (1986) (discriminating against interstate commerce in favor of in-state interests is unconstitutional); *Lewis v. BT Inv. Managers Inc.*, 447 U.S. 27, 43-44 (1980) ("[T]he Commerce Clause prohibits a State from using its regulatory power to protect its own citizens from outside competition."). In general, legal commentators have recognized the protectionist nature of state takeover statutes. See, e.g., Langevoort, *supra* note 455, at 107; Macey, *supra* note 457, at 478-79; Oesterle, *supra* note 451, at 937-38; cf. Coffee, *supra* note 454, at 437-38 (recognizing that a state cannot embargo the transfer of jobs or assets out of state and arguing that state takeover statutes therefore seek to accomplish indirectly what a state would be prohibited under the commerce clause from doing directly). Two commentators have suggested that states concerned about the local effects of plant closings and employee layoffs could enact legislation having a milder impact on interstate commerce—plant closing legislation requiring advance notice of closings, severance pay, and job retraining. See Bamonte, *The Dynamics of State Protectionism: A Short Critique of the CTS Decision*, 8 N. ILL. U.L. REV. 259, 263 (1988); Oesterle, *supra* note 451, at 939.

468 Justice Powell, who wrote the majority opinion in *CTS*, apparently believes that a protectionist purpose is permissible. He never said so in *CTS*, but his concurring opinion in *MITE* is revealing on this point. See *Edgar v. MITE Corp.*, 457 U.S. 624, 646 n.* (1982) (Powell, J., concurring) ("When corporate headquarters are transferred out of a city and State . . . , the State and locality from which the transfer is made inevitably suffer significantly.").

the Indiana statute is objectionable under the commerce clause.⁴⁶⁹

C. State Takeover Legislation After CTS

The state legislatures could not miss the official announcement contained in the *CTS* opinion. Those states that had adopted control share acquisition statutes had been successful in eschewing the constitutional infirmities of the first-generation takeover statutes. As one might expect, after *CTS* there was a spate of new control share acquisition laws, usually patterned after the Indiana statute, and today twenty-five states have control share acquisition statutes on the books.⁴⁷⁰ The most recent one is the Pennsylvania statute,⁴⁷¹ which adds a novel twist to the Indiana model. In brief, the Pennsylvania statute provides that short-term holders of target shares,⁴⁷² like offerors and target managers, are not entitled to vote their shares on the resolution regarding the restoration of voting rights to the control shares.⁴⁷³ This new feature makes the Pennsylvania control share acquisition statute the most potent one in the nation because it greatly decreases the likelihood of a shareholder vote favoring the offeror. The Pennsylvania legislature obviously realized that once an offer is launched large blocks of target shares are acquired by arbitrageurs and that arbitrageurs, if given the right to vote on the enfranchisement issue, will most likely vote in favor of the offeror.

469 Two commentators have suggested that if the *CTS* Court had balanced the burdens imposed on interstate commerce by the Indiana statute against the statute's local putative benefits, as the *MITE* Court had done in evaluating the Illinois statute, there would have been little to weigh in the state's balance. See Bamonte, *supra* note 467, at 266; Cox, *supra* note 448, at 361.

470 See *infra* note 482.

471 Pennsylvania Takeover Act of 1990, Act No. 1990-36, § 6, 1990 Pa. Legis. Serv. 93, 101-09 (Purdon) (to be codified at 15 PA. CONS. STAT. §§ 2561-2567).

472 *Id.* at 103-04 (to be codified at 15 PA. CONS. STAT. § 2562). Under the statute, a short-term holder is any shareholder who purchases target shares during the period commencing on the fourth business day prior to the first date on which public disclosure is made of a proposed control share acquisition and ending on the record date of the shareholder meeting at which shareholders will consider whether voting rights will be restored to the control shares.

473 This aspect of Pennsylvania's control share acquisition statute appears to run afoul of rule 19c-4, 17 C.F.R. § 240.196-4 (1990), which prohibits a national securities exchange from listing (and NASD from authorizing for quotation) the equity securities of any company that imposes a restriction on the voting power of its common stock based on the length of time a shareholder has held the stock. Rule 19c-4, however, was recently declared invalid by the Court of Appeals for the District of Columbia Circuit. See *Business Roundtable v. SEC*, 905 F.2d 406 (D.C. Cir. 1990).

To supplement the control share acquisition legislation, Pennsylvania simultaneously adopted a controversial disgorgement statute which is entirely different from all other state takeover legislation.⁴⁷⁴ This disgorgement statute allows a Pennsylvania corporation (or a shareholder suing on behalf of the corporation) to recover certain profits realized by a "controlling person" upon the sale of the corporation's equity securities to the corporation or a third party. The profits are recoverable if the sale occurs within eighteen months after the person became a "controlling person" and the securities were acquired within twenty-four months before or eighteen months after the person became a "controlling person."⁴⁷⁵ A "controlling person" is defined as (1) any person who has acquired, offered to acquire, or publicly disclosed an intention to acquire at least twenty percent of the voting power of a Pennsylvania corporation or (2) any person who has publicly disclosed that it "may seek" to acquire the power to direct the management and policies of a Pennsylvania corporation.⁴⁷⁶ The Pennsylvania disgorgement provision is ostensibly designed to address the problem of speculators who seek to put a corporation "in play" by initiating or announcing a takeover attempt (even though they have no interest in acquiring control) so that they will be able to make short-term profits on the sale of their shares once the price has risen.⁴⁷⁷

474 Pennsylvania Takeover Act of 1990, Act No. 1990-36, § 6, 1990 Pa. Legis. Serv. 93, 109-14 (Purdon) (to be codified at 15 PA. CONS. STAT. §§ 2571-2575). The disgorgement statute is modeled on § 16(b) of the Exchange Act, 15 U.S.C. § 78p(b) (1988).

475 Pennsylvania Takeover Act of 1990, Act No. 1990-36, § 6, 1990 Pa. Legis. Serv. 93, 113-14 (Purdon) (to be codified at 15 PA. CONS. STAT. §§ 2574-2575).

476 *Id.* at 111-12 (to be codified at 15 PA. CONST. STAT. § 2573).

477 As part of its 1990 takeover legislation, Pennsylvania also enacted a stakeholder provision that allows directors of Pennsylvania corporations, when taking action in response to a tender offer, to consider the effects the offer may have on constituencies other than shareholders, such as employees, suppliers, customers, creditors, and the communities in which the corporation is located. The provision also adds the statement that "directors . . . shall not be required . . . to regard any corporate interest or interests of any particular group affected by such action as a dominant or controlling interest or factor." *Id.* § 4, 1990 Pa. Legis. Serv. at 97 (to be codified at 15 PA. CONS. STAT. § 1721(e)).

Pennsylvania corporations otherwise covered by the three new provisions are permitted to opt out of each provision by a bylaw amendment adopted by the board of directors within 90 days of the effective date of the statute. *Id.* §§ 4, 6, 1990 Pa. Legis. Serv. at 99, 101, 109 (to be codified at 15 PA. CONST. STAT. §§ 1721(j), 2561(b), 2571(b)). Pennsylvania's 1990 takeover legislation did not turn out to be as popular as the legislature thought it would be. By July 26, 1990 (90 days after the effective date of the statute), approximately 40% of Pennsylvania corporations covered by the statute had

On the day they were enacted, Pennsylvania's control share acquisition and disgorgement statutes were challenged on constitutional grounds in federal district court.⁴⁷⁸ A definitive judicial opinion, however, has not yet been rendered.⁴⁷⁹ The *CTS* Court's receptiveness to state takeover legislation suggests that both statutes will ultimately be sustained, but they should not be. The Pennsylvania legislation, which is unquestionably biased in favor of incumbent management (considerably more so than the Indiana statute), upsets the careful balance between offerors and target management established by the Williams Act and, therefore, should be preempted. Moreover, the disgorgement provision is overbroad—it deters even bona fide bidders from making offers, to the detriment of target shareholders. In addition, both provisions appear to have been prompted by a desire to make Pennsylvania corporations takeover proof. If so, such a motive is strong evidence that the provisions have an economically protectionist purpose, and as argued above, protectionist state legislation offends the commerce clause. Finally, the disgorgement provision does not govern the internal affairs of Pennsylvania corporations but instead impermissibly burdens interstate commerce by regulating the disposition of profits earned from interstate transactions, even when the transactions have no contact with Pennsylvania.

Other states besides Pennsylvania have come to realize that in the post-*CTS* era control share acquisition legislation based on the Indiana model, although sound from a constitutional standpoint, may not be a strong enough deterrent to hostile bids.⁴⁸⁰ Yet,

opted out of at least one of the three provisions. See *Philadelphia Inquirer*, July 26, 1990, at A18, col. 1.

478 *Armstrong World Indus. v. Adams*, No. 90-2920 (E.D. Pa. filed Apr. 27, 1990); *First City Fin. Corp. v. Armstrong World Indus.*, No. 90-2922 (E.D. Pa. filed Apr. 27, 1990).

479 See *First City Fin. Corp. v. Armstrong World Indus.*, No. 90-2922 (E.D. Pa. June 15, 1990) (order dismissing complaint with prejudice).

480 Ohio might be considered an exception. In 1990, Ohio amended its control share acquisition statute (see *supra* note 418) by adding a provision similar to the novel provision contained in Pennsylvania's new control share acquisition statute. Ohio's amended statute, however, differs from the Pennsylvania statute in that a purchaser of target shares is not treated as a short-term "interested" shareholder unless the shares are purchased on or after the date of the first public disclosure of the control share acquisition. See Act effective Apr. 11, 1990, No. 180, § 1, 1990 Ohio Legis. Bull. 242, 244 (Anderson) (to be codified at OHIO REV. CODE ANN. § 1701.01). Apparently, the Ohio legislature was concerned that the Pennsylvania legislation might offend the due process clause by its classification of pre-disclosure purchasers as short-term "interested" shareholders. See *supra* note 472. Ohio also added a disgorgement provision that resembles the Pennsylvania statute, but it is not as broad. Significantly, the Ohio provision does

these states have not chosen to strengthen the Indiana model or search out entirely new forms of antitakeover measures as Pennsylvania has done.⁴⁸¹ Instead, they have adopted or modified existing fair price, cash-out, or business combination statutes, which are generally considered to be more effective than the standard control share acquisition statute.⁴⁸² Presently, nine states have fair price statutes, two states have cash-out laws, and twenty-eight states have some type of business combination legislation. Several states have enacted more than one of these statutes, and fair price, cash-out, and business combination statutes have frequently been coupled with a control share acquisition statute for good measure. In all, thirty-eight states have at least one of these four types of statutes in force,⁴⁸³ and California is the only major in-

not apply to a bidder who can establish either a bona fide intent to acquire control or a nonmanipulative purpose. See Act effective Apr. 11, 1990, No. 180, § 1, 1990 Ohio Legis. Bull. 242, 256-57 (Anderson) (to be codified at OHIO REV. CODE ANN. § 1707.043). Although both of Ohio's provisions were enacted into law approximately two weeks before the Pennsylvania legislation was adopted, the statutory concepts originated in Pennsylvania.

481 Delaware, for example, considered but rejected the idea of adopting a control share acquisition statute. See Stroufe & Gelband, *Business Combination Statutes: A "Meaningful Opportunity" for Success?*, 45 BUS. LAW. 891, 896-97 (1990).

482 See *supra* text accompanying notes 420-22. At the time Pennsylvania adopted the control share acquisition and disgorgement provisions, it also had fair price, cash-out, and business combination statutes in force. See 15 PA. CONS. STAT. ANN. §§ 1728, 2541-2553, 2554-2556 (Purdon 1990). A bidder's preference for the four types of second-generation statutes would probably have the following order: control share acquisition statute, fair price statute, business combination statute, cash-out statute. See Oesterle, *supra* note 451, at 881-82 & n. 20; Romano, *The Political Economy of State Takeover Statutes*, 43 VA. L. REV. 111, 148-69 (1987). But see Langevoort, *supra* note 455, at 113 n. 75 (contending that fair price statutes are less burdensome than control share acquisition statutes).

483 As of September 1, 1990, the list is as follows: Arizona, Florida, Hawaii, Idaho, Indiana, Kansas, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Missouri, Nebraska, Nevada, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, South Dakota, Tennessee, Utah, Virginia, and Wyoming (control share acquisition statutes); Connecticut, Florida, Georgia, Illinois, Louisiana, Mississippi, Pennsylvania, Washington, and Wisconsin (fair price statutes); Maine and Pennsylvania (cash-out statutes); Arizona, Connecticut, Delaware, Georgia, Idaho, Illinois, Indiana, Kansas, Kentucky, Maine, Maryland, Massachusetts, Michigan, Minnesota, Missouri, Nebraska, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Virginia, Washington, Wisconsin, and Wyoming (business combination statutes). See WINTER, ROSENBAUM, STUMPF & PARKER, *supra* note 417, § 1.2, at 7-12 (citing statutory provisions in effect as of May 1, 1989); ILL. ANN. STAT. ch. 32, par. 11.75 (Smith-Hurd 1990); Act effective Apr. 11, 1990, § 1, 1990 Ohio Legis. Bull. 242, 249-52 (Anderson) (to be codified at OHIO REV. CODE ANN. 1704.01-.07); Pennsylvania Takeover Act of 1990, Act No. 1990-36, § 6, 1990 Pa. Legis. Serv. 93, 101-09 (Purdon) (to be codified at 15 PA. CONS. STAT. §§ 2561-2567); R.I. GEN. LAWS § 7-5.2-1 to -8 (Supp. 1990); S.D.

corporating state that does not.

The judiciary has not yet had the occasion to rule on the validity of a fair price or cash-out statute. In contrast, a handful of business combination statutes have been challenged by offerors on constitutional grounds, and the lower federal courts, interpreting *CTS* broadly, have almost uniformly found the statutes to be valid.⁴⁸⁴ The analytical approaches the courts have taken vary, and as a result two lines of cases are beginning to develop. The two lines of analysis are best exemplified by opinions of the District Court for the District of Delaware⁴⁸⁵ and the Court of Appeals for the Seventh Circuit,⁴⁸⁶ upholding the Delaware and Wisconsin statutes⁴⁸⁷ respectively. The Wisconsin statute, enacted after *CTS*, is modeled on the business combination statute pioneered in New York⁴⁸⁸ but differs from the New York statute because the moratorium on business combinations

CODIFIED LAWS ANN. § 47-33-8 to -19 (Supp. 1990); WYO. STAT. §§ 17-18-101 to -104, -301 to -309 (Supp. 1990). It should be noted that business combination statutes in some states (Connecticut, Delaware, Georgia, Kansas, Maine, Massachusetts, Michigan, Minnesota, Nebraska, Washington, and Wyoming) do not have a fair price component, and that some states (Pennsylvania, Wisconsin) have adopted both a fair price statute and a business combination statute with a fair price component.

484 See, e.g., *Amanda Acquisition Corp. v. Universal Foods Corp.*, 877 F.2d 496 (7th Cir.) (Wisconsin statute), *cert. denied*, 110 S. Ct. 367 (1989); *Vernitron Corp. v. Kollmorgen Corp.*, No. 89-0241 (S.D.N.Y. Feb. 15, 1989) (LEXIS, Genfed library, Dist file) (New York statute); *West Point-Pepperell, Inc. v. Farley, Inc.*, 711 F. Supp. 1088 (N.D. Ga. 1988) (Georgia statute); *City Capital Assocs. v. Interco, Inc.*, 696 F. Supp. 1551 (D. Del.) (Delaware statute), *aff'd on other grounds*, 860 F.2d 60 (3d Cir. 1988); *RP Acquisition Corp. v. Staley Continental, Inc.*, 686 F. Supp. 476 (D. Del. 1988) (Delaware statute); *BNS Inc. v. Koppers Co.*, 683 F. Supp. 458 (D. Del. 1988) (Delaware statute). *But see RTE Corp. v. Mark IV Indus.*, No. 88-C-378 (E.D. Wis. May 6, 1988) (LEXIS, Genfed library, Dist file) (invalidating the Wisconsin statute), *vacated as moot*, [1987-1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,789 (E.D. Wis. June 22, 1988).

485 *BNS Inc. v. Koppers Co.*, 683 F. Supp. 458 (D. Del. 1988).

486 *Amanda Acquisition Corp. v. Universal Foods Corp.*, 877 F.2d 496 (7th Cir.), *cert. denied*, 110 S. Ct. 367 (1989).

487 DEL. CODE ANN. tit. 8, § 203 (Supp. 1988); WIS. STAT. ANN. § 180.726 (West Supp. 1989). In *CTS*, the SEC and the United States filed a joint brief arguing that the Indiana statute was invalid under the commerce clause. The United States, however, did not argue that the Indiana statute was invalid under the supremacy clause, and the SEC took no position on the preemption issue. Brief for the SEC and the United States as Amici Curiae at 8-12, *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69 (1987) (Nos. 86-71 and 86-97). In contrast, in cases challenging the Delaware and Wisconsin statutes, the SEC filed briefs arguing that the statutes violated both the commerce clause and the supremacy clause. See Brief of the SEC, Amicus Curiae, *RP Acquisition v. Staley Continental, Inc.*, 686 F. Supp. 476 (D. Del. 1988) (No. 88-190) (Delaware statute); Brief of the SEC, Amicus Curiae, *RTE Corp. v. Mark IV Indus.*, No. 88-C-378 (E.D. Wis. May 6, 1988) (LEXIS, Genfed library, Dist file) (Wisconsin statute), *vacated as moot*, [1987-1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,789 (E.D. Wis. June 22, 1988).

488 N.Y. BUS. CORP. LAW § 912 (McKinney 1986 & Supp. 1990).

between bidders and targets lasts three years rather than five. The Delaware statute, also a post-*CTS* enactment, resembles the Wisconsin statute but is less restrictive. Under both statutes, the three-year moratorium does not apply if the target board approves the business combination prior to the date the bidder consummates its offer.⁴⁸⁹ The Delaware statute, however, provides two other ways that a bidder may escape the moratorium: if the bidder obtains in its offer eighty-five percent of the target shares (excluding shares owned by director-officers and certain employee stock plans), or if the business combination is approved during the moratorium by the target board and two-thirds of the disinterested target shareholders.⁴⁹⁰

In its evaluation of the Delaware business combination statute, the District Court of Delaware used the same standard of dormant commerce clause scrutiny as the *CTS* Court and concluded that the Delaware statute did not impose an undue burden on interstate commerce.⁴⁹¹ The court's preemption analysis, however, was somewhat unique. On the one hand, the court recognized that the Delaware statute furthered the goals of the Williams Act by protecting target shareholders from the coercive aspects of some tender offers. On the other hand, the court observed that by limiting the number of tender offers that shareholders receive, the Delaware statute could also frustrate the purposes of the Act. In this regard, the court realized that business combination statutes could eliminate hostile offers entirely because they effectively deprive a bidder of "perhaps the most important fruit of gaining control"—a business combination.⁴⁹² The court resolved the tension between its two observations by focusing primarily on the exception in the Delaware statute for eighty-five percent share acquisitions. The court ultimately concluded that this exception saved the statute from preemption since it gave hostile offers for Delaware corporations "a meaningful opportunity for success," despite management opposition.⁴⁹³

In its examination of the Wisconsin business combination statute, the Seventh Circuit rejected the Delaware District Court's "meaningful opportunity for success" test—which would have in-

489 DEL. CODE ANN. tit. 8, § 203(a)(1) (Supp. 1988); WIS. STAT. ANN. § 180.726(2) (West Supp. 1989).

490 DEL. CODE ANN. tit. 8 § 203(a)(2)-(3) (Supp. 1988).

491 *BNS Inc. v. Koppers Co.*, 683 F. Supp 458, 472-73 (D. Del. 1988).

492 *Id.* at 468.

493 *Id.* at 469-72.

validated the Wisconsin statute under the supremacy clause—and adopted an even laxer preemption standard. In formulating the standard, the court considered discarding the plurality preemption opinion in *MITE* and made the argument that the Williams Act did not prevent the states from adopting laws that favor either offerors or target management.⁴⁹⁴ Like the *CTS* Court, the Seventh Circuit, however, “stopped short of [this] precipice” and opined instead that state takeover laws were preempted by the Williams Act only if they altered any of the procedures governed by the Act.⁴⁹⁵ Not persuaded that the Wisconsin statute tampered with the tender offer procedures established by federal law, the court concluded that the Wisconsin statute passed preemption muster.⁴⁹⁶ Nevertheless, the court expressed its belief that the statute harmed shareholders by restricting the number of tender offers they would receive. But, the court found that this harm had no bearing on the preemption issue since the Williams Act did not entitle shareholders to receive tender offers.⁴⁹⁷ Finally, the court declined to adopt a “meaningful opportunity for success” test as the standard for evaluating the Wisconsin statute under the commerce clause, concluding that “[t]he [C]ommerce [C]ause does not demand that states leave bidders a ‘meaningful opportunity for success.’”⁴⁹⁸

The Supreme Court denied certiorari to the decision of the Seventh Circuit.⁴⁹⁹ If another circuit, however, adopts the approach taken by the District Court of Delaware and declares a Wisconsin-type business combination statute invalid, the Supreme Court may decide to grant certiorari. If this happens, it seems likely that the Supreme Court will opt for the reasoning of the Seventh Circuit and reverse. Such a ruling by the Court would have the effect of validating *all* business combination takeover statutes, assuming, of course, that the legislation does not run afoul of the commerce clause. This prediction is not meant to

494 This argument has also been advanced by some legal commentators. See, e.g., Fischel, *supra* note 53, at 71-74; Johnson & Millon, *Misreading The Williams Act*, 87 MICH. L. REV. 1862 (1989) (arguing that Williams Act-preemption of state takeover legislation is based on a “mistaken reading” of the Act).

495 *Amanda Acquisition Corp. v. Universal Foods Corp.*, 877 F.2d 496, 503-04 (7th Cir.), cert. denied, 110 S. Ct. 367 (1989).

496 *Id.* at 504.

497 *Id.* at 500-02, 504-05.

498 *Id.* at 508-09.

499 *Amanda Acquisition Corp. v. Universal Foods Corp.*, 110 S. Ct. 367, denying cert. to 877 F.2d 496 (7th Cir. 1989).

suggest that business combination statutes should be upheld. Even if a business combination statute does not founder on a commerce clause argument, business combination legislation is in conflict with and frustrates the purposes of the Williams Act and, therefore, is preempted. By giving target management total or substantial power to veto business combinations that are usually essential to tender offers, business combination legislation has the potential to eliminate from the tender offer process the target shareholder choice contemplated by the Williams Act.

If tested, fair price and cash-out statutes—which nominally protect target shareholders from coercive bids—will probably be sustained, but like business combination statutes, they should not be. Irrespective of the merits of a commerce clause challenge, both types of statutes are void under the supremacy clause. Fair price statutes impose supermajority and fair price requirements for post-tender offer business combinations but then allow target management to waive these requirements. In taking such a regulatory approach, fair price statutes give target management too much power in negotiating with a bidder and, as a consequence, upset the equitable balance between the contending sides. Cash-out statutes require offerors in partial bids to purchase, upon demand, shares that were not even sought in the offer. This requirement has the effect of eliminating partial bids. The Williams Act clearly contemplates the use of partial bids as a method of obtaining control,⁵⁰⁰ and thus cash-out statutes conflict with federal law.

One final observation deserves mention. In the 1950s when proxy control contests were in fashion, the states respected the preemptive force of the federal proxy rules and did not experiment with their own regulation. In the 1960s and thereafter, when cash tender offers replaced proxy battles as the favored method of capturing corporate control, the states responded differently to the new phenomenon. State legislatures adopted two (and some would say three) generations of tender offer statutes. Furthermore, while the state tender offer statutes were multiplying, state proxy regulation remained a virtual void.⁵⁰¹ Before

500 For example, § 14(d)(6) of the Williams Act requires a bidder to purchase shares pro rata in partial bids.

501 An interesting exception is the proxy regulation in Alaska of native Alaskan corporations. See ALASKA STAT. § 45.55.139 (1986); ALASKA ADMIN. CODE tit. 3, § 08.315-.365 (July 1990); see also Comment, *State Regulation of Proxies in Alaska Native Corporations*, 12 UCLA-ALASKA L. REV. 69 (1982-1983). Congress, however, has specifically ex-

CTS, this asymmetry between the regulation of proxy contests and tender offers was explainable because it appeared to be only temporary. The states had simply exceeded their authority in attempting to regulate tender offers, and they were told so. After *CTS*, however, the asymmetry becomes difficult to understand, since it seems to be permanent.⁵⁰²

CONCLUSION

The Ninetieth Congress, in 1968, instituted a national policy for the regulation of tender offers. This federal policy sought to protect investors involved in tender offers and to preserve, through regulatory neutrality, the viability of the tender offer as a method of corporate acquisition. The legislation that embodied this policy—the Williams Act—was meant to have a substantial remedial component, a significant substantive dimension, and strong preemptive force. In its trilogy of tender offer cases decided under the Williams Act, the Supreme Court, however, has frustrated these legislative intentions by misconstruing the text and purposes of the Act. Consequently, the healthy development of federal tender offer policy has been paralyzed. *Piper* limited the right of tender offer participants to redress violations of the Act. *Schreiber* gutted the Act of most of its substantive content. And *CTS* weakened considerably the Act's preemptive capability.

Questions concerning the implication of private actions, the substantive scope of statutory provisions, and the preemptive au-

empted Alaska native corporations from the requirements of the federal securities laws. 43 U.S.C. § 1625 (1988).

502 If state legislatures conclude that proxy regulation at the state level is not preempted by the federal proxy rules and enact their own legislation, the asymmetry, of course, will be eliminated. Although the courts have generally held that the federal proxy rules have preemptive force, the strength of this force is beginning to be questioned indirectly. *Compare* *NUI Corp. v. Kimmelman*, 593 F. Supp. 1457 (D.N.J. 1984) (holding that a state statute that prohibited the acquisition of control of a public utility by means of a proxy campaign without the approval of a state utilities board was preempted by the federal proxy rules because it interfered with the neutrality of the federal rules), *rev'd on other grounds*, 765 F.2d 399 (3d Cir. 1985) *with* *Business Roundtable v. SEC*, 905 F.2d 406, 410-11 (D.C. Cir. 1990) (contending that the federal proxy rules are primarily—although not exclusively—concerned with disclosure). As a consequence, some state legislatures are starting to enact provisions that have an effect on proxy control contests, and these provisions conflict with the federal regulatory scheme. The recent Pennsylvania disgorgement provision (*see supra* text accompanying notes 474-77) is a prime example. The Pennsylvania statute, which classifies a person who launches a proxy contest for corporate control as a "controlling person," discourages and impedes such contests and thus tips the balance in favor of the incumbent directors.

thority of federal regulatory schemes are not wholly legal; they are also inherently philosophical. And the Supreme Court's examination of these questions in *Piper*, *Schreiber*, and *CTS* could provide no better proof, since in all three cases the Court's legal analysis was either shaped or bolstered by a distinct philosophy of federal-state relations. This philosophy, which has been shared in varying degrees by a majority of the members of the Burger and Rehnquist Courts, is grounded on the notion that federal law should be interpreted so that state law is not displaced on matters that have traditionally been the province of the states.⁵⁰³ The influence of this philosophy in *Piper*, *Schreiber*, and *CTS* is manifest. In *Piper*, the Court refused to imply a federal remedy for deception in deference to a state remedy for the tort of interference with a prospective advantage. In *Schreiber*, the Court declined to establish a federal standard of conduct for corporate fiduciaries and bowed to the business judgment rule of state corporation law. And in *CTS*, the Court failed to find a preemptive conflict between federal legislation and a state statute couched in terms of substantive corporation law.

Whatever merit this philosophy may have in the abstract, its influence on the Court's interpretation of the Williams Act in *Piper*, *Schreiber*, and *CTS* is disturbing. It has facilitated an emasculation of the Act and has allowed state law to acquire a prominence in tender offer regulation that Congress never contemplated or intended. The Burger and Rehnquist Courts would disagree and respond that if Congress had meant to limit the role of the states in regulating tender offers, Congress would have explicitly said so. But Congress' decision to remain largely silent is understandable. When Congress formulated its regulatory policy for tender offers, it did not feel pressed to anticipate the ramifications of state law because the philosophy of federalism held by the Warren Court at the time viewed federal legislation as a major restraint on the operation of state law.⁵⁰⁴ Thus, Congress assumed that a fairly comprehensive federal policy, of its own force, would inhibit the development of any competing state policies.

503 See *supra* text following note 197; *supra* text accompanying notes 230-31. See generally Note, *The Preemption Doctrine: Shifting Perspectives of Federalism and the Burger Court*, 75 COLUM. L. REV. 623, 639-53 (1975) (observing the Burger Court's solicitude of the states' interests in preemption cases).

504 See Note, *supra* note 503, at 638-39 (pointing out that the Court's shift in its philosophy of federalism occurred around 1973); *supra* note 141 and accompanying text; *supra* text following note 197.

Although Congress thought that the Williams Act would restrict the states' role in tender offer regulation, it did not intend to exclude the states entirely from the regulatory process nor did it fail to recognize the interstitial nature of federal law. Indeed, Congress seldom adopts a complete and self-sufficient body of law.⁵⁰⁵ Instances in which the Williams Act countenances or relies on state law have already been mentioned. First, the "savings clause" contained in section 28(a) of the Exchange Act preserves the rights and remedies of existing state law and allows concurrent state tender offer regulation as long as it does not conflict with the federal scheme.⁵⁰⁶ This clause would permit, therefore, parallel or partly parallel state actions for deceit, interference with a prospective advantage, and breaches of the duty of care or loyalty. Furthermore, state tender offer disclosure statutes, which are in effect in many states today,⁵⁰⁷ would survive preemption scrutiny by virtue of this clause, since they supplement, rather than obstruct, the operation of the federal statute. Second, the Williams Act implicitly adopts the state law of contracts as the body of law for determining the contractual rights and remedies of the offeror and target shareholders. This body of law, however, has been modified in certain respects by the substantive provisions of the Act.⁵⁰⁸

Suffice to say that this congressional vision of the relationship between federal and state law in the regulation of tender offers is a far cry from the relationship that exists today. State law has been allowed to shape the substantive aspects of tender offer regulation, while the Williams Act takes a back seat as a disclosure statute. State policy—or perhaps one should say the policy of Delaware (approximately one-half of all New York Stock Exchange-listed companies are incorporated there)⁵⁰⁹—has become the national policy.

If today's Congress were to evaluate the Williams Act, it

505 Hart, *The Relations Between State and Federal Law*, 54 COLUM. L. REV. 489, 498 (1954).

506 See *supra* note 397 and accompanying text.

507 See, e.g., ARK. STAT. ANN. §§ 23-43-101 to -117 (1987); CONN. GEN. STAT. ANN. §§ 36-456 to -468 (West 1987 & Supp. 1990); IND. CODE ANN. § 23-2-3.1-0.5 to -2-3.1-11 (West 1989 & Supp. 1990); MASS. ANN. LAWS ch. 110C, §§ 1-13 (Law. Co-op. 1985); N.J. STAT. ANN. §§ 49:5-1 to -19 (West Supp. 1990); N.Y. BUS. CORP. LAW §§ 1600-1613 (McKinney 1986); TENN. CODE ANN. §§ 48-35-101 to -113 (1988 & Supp. 1990); see also notes 211-13 and accompanying text.

508 See *supra* text accompanying notes 354-58.

509 See Johnson & Millon, *supra* note 494, at 1862.

would find that the premises and purposes which the Act incorporates are as necessary and as appropriate today as they were in 1968. Congress would reach this conclusion because its deliberations would reveal the following: First, the need for governmental action to protect investors involved in tender offers has not changed. Second, tender offers can be beneficial to target shareholders and therefore investor protection should be accomplished by a set of legal rules that do not impair the vigor of the tender offer process. Third, the viability of the tender offer device can be preserved only if the legal rules are neutral as between the bidder and target management. And finally, neutrality can be achieved only at the federal level and only with legislation that curtails the role of state law, since state law consistently evinces a distinct promanagement bias.⁵¹⁰

A legislature that would give its stamp of approval to the design Congress envisioned for tender offer regulation in 1968 would necessarily conclude that *Piper*, *Schreiber*, and *CTS* should not be left intact. Indeed, as this Article has argued, the Supreme Court's pronouncements in these three cases are at loggerheads with Congress' plan. The recommendation of this Article is therefore plain. Congress should negate *Piper*, *Schreiber*, and *CTS*. In addition to resurrecting the intentions of the Congress that enacted the Williams Act, such action would have two other desirable effects. First, it would result in uniform tender offer regulation.

510 Scholars of law and economics generally argue that entrepreneurs choosing a state of incorporation will search for a state that has a package of legal rules that maximizes shareholder welfare and that states will adopt rules that are in the interest of shareholders in order to compete for the revenues produced by incorporations. These scholars have therefore concluded that federal chartering of corporations or the establishment of federal standards of fiduciary conduct would be undesirable for economic reasons. This view was first proposed by Professor Winter, see Winter, *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251 (1977), and it has been subsequently advanced by others, see Easterbrook, *Managers' Discretion and Investors' Welfare: Theories and Evidence*, 9 DEL. J. CORP. L. 540 (1984); Fischel, *The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware's Corporation Law*, 76 NW. U.L. REV. 913 (1982). As two legal commentators have observed, the law and economics scholars were "hoisted by their own petards" when the states adopted "antitakeover" statutes since economic studies generally conclude that takeovers are beneficial to shareholders and the economy. See Johnson & Millon, *supra* note 494, at 1881-82. Indeed, Professor Winter himself recognized the problem that state takeover statutes pose for his view and therefore called for their elimination. See Winter, *supra*, at 287-89 (analyzing first-generation statutes). Accepting Professor Winter's view of state takeover statutes, one commentator has argued that economic analysis also calls for federal (and not state) law to govern the defensive conduct of target management. See Fiflis, *supra* note 256, at 330-31.

And second, it would put tender offers and proxy battles on a par from a regulatory perspective and thus place both methods of capturing corporate control chiefly within the sphere of federal governance.

Negating the Supreme Court's three tender offer cases would not require elaborate legislation. *Piper* could be nullified by adding a subsection to the Williams Act that gives parties injured by violations of the Act the express right to sue in law or equity. In 1988, Congress took similar action in the area of insider trading by creating an express private action for damages to redress certain violations of rule 10b-5.⁵¹¹ *Schreiber* could be overturned by defining the phrase "manipulative acts or practices" in section 14(e). The definition would provide that section 14(e) manipulative conduct encompasses, but is not limited to, unfair practices that coerce or prevent the investment decisions of shareholders involved in tender offers. This definition would make most defensive measures taken by target companies unlawful and would therefore limit the significance of the common-law business judgment rule as a standard for reviewing the conduct of target directors seeking to resist a takeover attempt. Front-end loaded, two-tier offers would also be illegal under the definition. Other partial offers, however, would not be illegal since they are not structurally coercive. Finally, *CTS* could be voided by amending the Exchange Act with a provision that specifically preempts the various types of state "antitakeover" statutes currently on the books and that gives the SEC the authority to preempt other antitakeover strategies that might be devised by the states in the future.

The above recommendations for congressional action do not protect target shareholders from the potentially coercive nature of partial offers; furthermore, the proposals tie the hands of target managers and state legislators who have ostensibly acted to provide such protection. If legislators perceive this gap in shareholder protection to be significant, Congress should consider the following additional amendment. Offerors who make partial bids must pay a fair price (a price that at least equals the bid price) to target shareholders in any second-step business combination consummated during the two-year period after the termination of the offer. This amendment may have some appeal for two reasons. It

511 The express remedy is contained in § 20A of the Exchange Act, 15 U.S.C. § 78t-1 (1988), and it was created when Congress adopted the Insider Trading and Securities Fraud Enforcement Act of 1988, Pub. L. No. 100-704, § 5, 102 Stat. 4677, 4680-81.

gives a nod to the states by recognizing the utility of one of their ideas. Also, it furthers the federal goal of investor protection by extending the equal treatment of tendering shareholders to all shareholders without unduly tipping the scales.

The possibility that Congress and state legislatures will take dissimilar approaches to the same problem is inherent in federalism. In the case of tender offer regulation, the possibility has occurred. This Article has expressed one view on how Congress should reconcile these divergent approaches. It is hoped that Congress shares this view and has the conviction to act on it.