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Efficient Capital Market Theory, the Market for Corporate Control, and the Regulation of Cash Tender Offers

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Federal and state regulation of the cash tender offer makes it difficult for outsiders to win control of a corporation whose securities have been doing poorly in the capital market. Mr. Fischel argues that efficient capital market theory undermines the reasons usually given for these regulatory barriers, and concludes that without these barriers the efficiency of the related market for corporate control would improve. His discussion also examines the courts' use of the business judgment rule in cases charging that managers have improperly dedicated corporate funds to measures that discourage tender offers, and extolls instead the recently devised compelling business purpose test, which shifts the burden of justification to defendant managers.

I. Introduction

On the basis of empirical and theoretical work of recent decades, the thesis that capital markets like those provided by our national stock exchanges are allocationally efficient has gained increasing support. In general terms, a capital market is efficient in this sense if the prices of traded securities accurately and promptly reflect the securities' intrinsic values relative to all publicly available information, or in other words, if the market responds immediately to relevant information that any trader may have and never attaches the wrong evidentiary weight to the information. One of the factors that will be reflected in the price of a firm's securities in an efficient capital market is the capability of its current management. If a firm is poorly managed, the price of its se-

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curities will be lower than under more competent management, and the firm and society in general would benefit from a transfer of control to more capable managers.[1] The informational efficiency of a securities market does not, however, imply the existence of a corresponding market for corporate control, a mechanism permitting control to shift from one group of managers to another group that can employ the assets of a corporation more profitably.

Corporate control can change hands in several ways, but the most effective means now available for wresting control from a resisting management, the means most favored by aggressors, is the cash tender offer.[2] The essence of the cash tender offer is the offeror's public invitation to all shareholders of the target company to tender their shares at a specified price within a specified time.[3] The tender offer price will generally be considerably above the market price of the securities at the time of the offer. The tender offeror may seek to acquire all the target company's shares or only a fixed number less than the total amount outstanding. The offeror is usually willing to pay a premium to acquire control in the belief that it can manage the target company more efficiently than present management. The cash tender offer thus provides a mechanism for transfer of control to those who believe they can better manage the assets of the corporation. Target managements, however, frequently resist tender offers because a change in control is likely to herald a forced change in management. Although the defending management usually attempts to justify its tactics as being in the best interests of shareholders, several shareholder suits have recently challenged management resistance to takeover bids.[4]

Cash tender offers are subject to pervasive federal and state regulation. Under federal law, the Williams Act[5] imposes various filing, disclosure, and other requirements on tender offerors. The Act also partially regulates the conduct of target management.[6] Approximately half the states have enacted statutes that supplement the provisions of

1. For an excellent summary of efficient capital market theory and relevant literature, see J. LORIE & M. HAMILTON, THE STOCK MARKET: THEORIES AND EVIDENCE 70-97 (1973). *See also* notes 9-12 *infra* & accompanying text.

2. P. DAVEY, DEFENSES AGAINST UNNEGOTIATED CASH TENDER OFFERS 1-4 (National Indus. Conf. Bd. Rep. No. 726, 1977).

3. The application of the term "tender offer" is unsettled. *See* E. ARANOW, H. EINHORN, & G. BERLSTEIN, DEVELOPMENTS IN TENDER OFFERS FOR CORPORATE CONTROL 1-35 (1977).

4. For a list of these cases, see Nathan & Kapp, *Recent Developments Under the Williams Act in Takeover and Acquisitions*, 9 REV. SEC. REG. 261, 285 (1977).

5. 15 U.S.C. §§ 78g, *l*-n, s (1976), *as amended by* Foreign Corrupt Practices Act of 1977, Pub. L. No. 95-213, 91 Stat. 1494 (1977).

6. 15 U.S.C. § 78n(d)(4), (e) (1976).

the Williams Act.[7] Under state common law, directors and officers owe shareholders a fiduciary duty which further governs the propriety of management defensive tactics.[8]

This Article argues that efficient capital market theory undermines the supposed justification for current tender offer regulation and legal defensive tactics available to target company management. The Article further argues that federal and state regulation of cash tender offers coupled with the defensive tactics available to target management operate to frustrate the effective functioning of the market for corporate control to the detriment of all shareholders. Part II introduces the essentials of efficient capital market theory and explains the notion of the market for corporate control, two topics necessary for a theoretical understanding of the role of the cash tender offer. The Williams Act and its effect on cash tender offers are the focus of Part III. Part IV examines the effect of state tender offer statutes. The array of defensive tactics available to incumbent management are discussed in Part V. Finally, Part VI proposes a revised standard of fiduciary duty that management defensive tactics should satisfy.

II. Efficient Capital Market Theory and the Market for Corporate Control

A. *Efficient Capital Market Theory*

An efficient capital market[9] is one in which a trader cannot im-

7. *See* notes 89-94 *infra* & accompanying text.
8. *See* notes 116-18 *infra* & accompanying text.
9. Two major implications of efficient capital market theory are that (1) security prices adjust rapidly and in an unbiased manner to any new information, and (2) price changes behave in a random manner. B. LEV, FINANCIAL STATEMENT ANALYSIS: A NEW APPROACH 212 (1974). If prices of securities did not adjust rapidly and without bias, investors could profit by trading during the time during which securities did not reflect all available information or during periods when the market either overcompensated or undercompensated for new information. Similarly, if security prices did not move randomly, investors could capitalize on systematic price movements to earn above average returns.

The empirical support for efficient capital market theory exists in three forms—weak, semi-strong, and strong. The weak form has focused on the significance of securities' past price movements. Repeated studies have demonstrated that historic patterns of past prices are of no value in predicting future price movements. The semi-strong form asserts that security prices reflect all publicly available information about that security. Empirical tests of the semi-strong form have tested the speed of adjustment of security prices to such events as stock splits, annual earnings announcements and large secondary offerings of common stock. These tests indicate a quick price adjustment process in which the information revealed by specific events is anticipated by the market. The strong form of efficient capital market theory is that even nonpublic information is quickly reflected in security prices. Tests of the strong form have proven inconclusive. Several studies of professionally managed mutual funds have concluded that these funds, despite huge expenditures to identify mispriced securities, were unable to consistently outperform the market. Other studies have found, however, that corporate insiders can profit by trading on inside information not available to other investors.

prove his overall chances of speculative gain by obtaining public information about the companies whose securities are in the market and evaluating that information intelligently in determining which stocks to buy and sell. Paradoxically, the efficiency of the market results from the competitive efforts of securities analysts and investors who strive to earn superior returns by identifying mispriced securities—securities that are either overvalued or undervalued. The goal of securities analysis is to discover information that suggests differences between current market prices and what these prices "should" be, the securities' intrinsic values. The securities analyst acts on this information by buying, selling, or recommending securities. The process ensures that market prices reflect all available information. Insider trading—trading by individuals with access to "inside" or nonpublic information—also contributes to market efficiency. Legal constraints on insider trading preclude or at least impede insider trading, thereby creating some market inefficiency. Nevertheless, in an efficient capital market in which a large number of buyers and sellers react through a market mechanism such as the New York Stock Exchange to cause market prices to reflect fully and instantly all available information about a company's securities, investors should not be able to "beat the market" systematically by identifying undervalued or overvalued securities.

While efficient capital market theory has many implications for securities regulation,[10] including certain aspects of tender offer regulation to be discussed later, my present concern is with its implications for an allocationally efficient stock market. The efficiency of the securities markets is typically appraised in terms of both operational and allocational efficiency. Operational efficiency refers to the costs of issuing or transferring securities. These costs include underwriting and other flotation costs of new issues as well as transaction and regulatory costs in public transfers of outstanding issues. Allocational efficiency, generally considered the most important economic goal achieved by securities markets, refers to the ability of those markets to maintain equivalent rates of return or costs of financing on comparable invest-

For a survey of the literature on the empirical support for efficient capital market theory, see J. LORIE & M. HAMILTON, *supra* note 1, at 87-96; Note, *The Efficient Capital Market Hypothesis, Economic Theory and the Regulation of the Securities Industry*, 29 STAN. L. REV. 1031, 1041-54 (1977).

10. *See, e.g.*, Langbein & Posner, *Market Funds and Trust-Investment Law*, 1976 AM. BAR FOUNDATION RES. J. 1 (implications for portfolio theory and duties of a trustee); Langbein & Posner, *Market Funds and Trust-Investment Law* II, 1977 AM. BAR FOUNDATION RES. J. 1 (implications for portfolio theory and duties of a trustee); Note, *The Efficient Capital Market Hypothesis*, *supra* note 9, at 1069-76 (implications for SEC disclosure requirements and regulation of insider trading).

ments with equivalent risks.[11] In an efficient capital market, all information about a company's securities is reflected in their price, making the prices of securities the best available indicators of their value. As such, "prices are accurate signals for capital allocation."[12] Companies whose securities offer the same level of risk have equal access to new funds at the same costs; more profitable investments are able to bid investment dollars away from investments offering a lower rate of return. Differences in return on comparable investments are no more than those justified by their differences in risk.

B. The Market for Corporate Control

Efficient capital market theory implies that if a publicly traded company is poorly or less than optimally managed, the price of its securities will reflect this fact accurately and promptly. That a capital market is efficient, however, does not imply that there is a similarly efficient mechanism whereby control shifts from less capable managers to others who can manage corporate assets more profitably. The market for corporate control, so called by Henry Manne in his groundbreaking work on the subject,[13] must perform that function in our economic system.

Poor performance of a company's securities in the capital market is a common indication of poor management. The lower the market price of the securities compared to what it would be with better management, the more attractive the firm is to outsiders with the ability to take the firm over. The most common takeover device is the merger. This takeover device is not available, however, when incumbent management opposes the shift in control because merger statutes uniformly require approval by the directors of the two corporations.[14] The two techniques that can be used to shift control when there is opposition are the direct purchase of shares and the proxy contest.

Direct purchases of shares can be purchases as a result of private negotiations with large individual shareholders, open market purchases, or purchases pursuant to a tender offer. The first type of direct purchase has the advantages of secrecy and price negotiation. From a practical point of view, this type of direct purchase is highly

11. Friend, *The SEC and the Economic Performance of Securities Markets*, in ECONOMIC POLICY AND THE REGULATION OF CORPORATE SECURITIES 190 (H. Manne ed. 1960).

12. E. FAMA, FOUNDATIONS OF FINANCE 133 (1976).

13. *E.g.*, Manne, *Cash Tender Offers for Shares—A Reply to Chairman Cohen*, 1967 DUKE L.J. 231; Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110 (1965).

14. *See, e.g.*, TEX. BUS. CORP. ACT ANN. art. 5.03A (Vernon 1956).

desirable if there are at most a few controlling shareholders.[15] Open market purchase of shares can also be an effective takeover device. The Securities Exchange Act of 1934 requires, however, that a statement be filed with the Securities Exchange Commission (SEC) within ten days after the purchase of five percent of any class of equity security.[16] This disclosure will fuel the inevitable rise in market price that occurs when news spreads that there is a buyer in the market seeking control, making this form of direct purchase prohibitively expensive if shares are widely dispersed.

The tender offer is the most advantageous means of acquiring control if shares are widely held. Unlike open market purchases which may leave an offeror in a minority position if it acquires insufficient shares, a tender offer can be conditioned on receiving sufficient shares for control. The offeror can specify other terms of the offer such as the offer price, the length of time during which the offer will remain open, and withdrawal rights. Compensation for tendered shares can either be cash or a package of securities of the offeror. But a stock tender offer has significant drawbacks if incumbent management opposes a shift in control. The Securities Act of 1933 requires that all new securities offered for sale be registered. This registration provides management with advance warning of any takeover bid and thereby denies the offeror the element of surprise generally necessary for a successful tender offer.[17]

The alternative way to shift control in the face of hostile management is the proxy fight. The expense entailed in the solicitation of proxies and compliance with SEC disclosure regulations makes waging a proxy contest extremely costly. While SEC regulations have also made tender offers more expensive, an important difference still exists. If an outsider loses a proxy fight, it may have little or nothing to show for its expenses; a defeated tender offeror, in contrast, will at least own tendered shares if control is not obtained.[18] Finally, the probability of an outsider's success in a proxy fight is far less than that of his success

15. Several commentators, however, contend that control is a corporate asset and therefore all shareholders are entitled to share in any premium paid for control. *E.g.*, Jennings, *Trading in Corporate Control*, 44 CALIF. L. REV. 1, 9 (1956). This rule would have the undesirable effect of frustrating shifts in corporate control to individuals who might use their controlling influeuce to operate the corporation more efficiently, thereby benefitting all shareholders.

16. 15 U.S.C. § 78m(d)(1) (1970), *as amended by* Pub. L. No. 95-213, § 202, 91 Stat. 1494 (1977).

17. If the offeror loses the element of surprise, management has the opportunity to employ a wide variety of defensive tactics to defeat the tender offer. *See* Part V *infra*.

18. The offeror, of course, is free to condition its offer on gaining enough shares to ensure control.

in a tender offer because of management's well-known dominance of the proxy machinery. The superior opportunity presented to a shareholder in a tender offer—the immediate opportunity to sell his shares at a premium above market price versus the almost impossible task of evaluating complex arguments compressed into proxy materials—strongly suggests the superiority of the tender offer as a takeover device.

C. Characteristics of Target Companies

A key assumption about the market for corporate control is that outsiders are attracted to firms that are poorly managed. Empirical evidence supports this assumption. Studies designed to uncover the typical traits of target companies generally conclude that poor management performance is a common characteristic.[19] This conclusion finds corroboration in efficient capital market theory. Because the market prices of securities faithfully reflect value, other explanations for the takeover attractiveness of target companies that assume frequent aberrations in stock market valuations are suspect.[20] While the evidence

19. The result of a detailed study of fifty tender offers over a ten year period, for which the underlying data was not published, was that "[t]he typical subject company has exhibited disappointing operating performance, paid decreasing dividends and is excessively liquid. In short, vulnerability to a take-over bid may be traceable to inept, or at least overly-conservative management." Taussig & Hayes, *Are Cash Takeover Bids Unethical?*, 23 FINANCIAL ANALYSTS' J. 107, 108 (1967). A second study also found that target companies do not perform as well as comparable companies in their industries. Austin & Fishman, *The Tender Take-Over*, MERGERS & ACQUISITIONS, May-June 1969, at 4. Focusing on 104 tender offers from 1956 to 1965, this study revealed that 83.8% of target companies had profit margins equal to or lower than other firms in their respective industries. Similarly, 86.1% of target companies yielded either no more or even less to the equity owners than comparable firms. Of all target companies, 65.8% evideuced either decreasing or steady stock price performance. Other characteristics of the target companies were below industry performance in sales and earnings, poor divideud policy, book values frequently above share price, and excessive liquidity. The authors conclude that target firms have been "operating in a retrograde manner relative to their competitors." *Id.* at 6. One empirical study based on an examination of eighteen tender offers during the first six months of 1967 reached a contrary couclusion. Comment, *Economic Realities of Cash Tender Offers*, 20 ME. L. REV. 237 (1968). Studies of takeovers in the United Kingdom have been divided on the issue of poor performance by target companies. *Cf.* A. SINGH, TAKEOVERS (1971) (finding no high correlation between low profitability and susceptibility to takeover attempts); D. KUEHN, TAKEOVERS AND THE THEORY OF THE FIRM 83, 110 (1975) (finding such a correlation).

The thesis that the attractiveuess of companies to tender offerors has no correlation with poor performance but does reflect the market's undervaluing of the companies' securities as reflected in the securities' low price-earnings ratios is part of the lore advanced by managements that face unwelcome tender offers. This lore surfaces in works of advice to the threatened managers. *See, e.g.*, P. DAVEY, *supra* note 3, at 6; Lee, *Tender Offer Defenses: How to Short-circuit the Corporate Raider*, MERGERS & ACQUISITIONS, Fall 1975, at 4, 6.

20. Efficient capital market theory suggests that the poor performance theory of target companies closely approximates reality. In an efficient capital market, disparities between market price and intrinsic value (the basic predicate of the *Maine Law Review* study, Comment, *supra* note 19) will rarely exist, or more accurately, will rarely be identifiable by investors. A distinction must be drawn between a firm that is undervalued and one that could be more profitable with

does not establish that acquisitions or mergers pursuant to tender offers invariably lead to more profitable performance, the willingness of offerors to pay a premium for control is some assurance that they strongly anticipate greater profitability.[21]

D. A Note on the Separation of Ownership and Control

One of the basic themes of corporation law is the significance for shareholders of the modern corporation's separation of ownership and control. In their famous work on this subject, Professors Berle and Means assumed that managers do not seek to maximize what is most important to shareholders—appreciation of the shareholders' underlying investment.[22]

Berle and Means failed to recognize, however, that unity of ownership and control is not a necessary condition of efficient performance of a firm.[23] If the owner of a wholly owned firm is its manager, he will make operating decisions that maximize his utility.[24] After the owner-manager sells equity in the firm to raise capital, however, his incentive to search out new profitable ventures diminishes because he now bears only a fraction of the losses resulting from less profitable investments.[25] The agency relationship between shareholders and managers inevitably calls into question the identity of the agent's decisions with decisions that would maximize the welfare of shareholders.[26]

Various market mechanisms exist, however, to minimize this divergence of interests between managers and shareholders. As Alchian has illustrated,[27] an architect or builder does not share in its profits or losses (as only the owners do) absent contractual arrangement. Yet the architect or builder is vitally interested in the success of the building. The greater the profits generated by his efforts, the greater the demand for his services. Corporate managers are in precisely the same situa-

different management. The first situation is highly unlikely in an efficient capital market. But it is entirely possible that a share price reflects all available informatiou about a company, yet is far lower than what it would be under different management.

21. *See, e.g.*, P. DAVEY, *supra* note 2, at 6; Lee, *supra* note 19, at 4, 6.

22. A. BERLE & G. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (rev. ed. 1968).

23. *See, e.g.*, R. POSNER, ECONOMIC ANALYSIS OF LAW 301 (2d ed. 1977).

24. Jensen & Meckling, *Theory of the Firm: Managerial Behavior: Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 312 (1976).

25. Similarly, as the owner-manager's share of the equity falls and his fractional claim on the outcome falls, he will have greater incentives to appropriate larger amounts of corporate resources in the form of perquisites. *Id.* at 313.

26. In addition to this inevitable residual loss, other costs of the agency relationship are monitoring expenditures by the principal and bonding expenditures by the agent. *Id.* at 308.

27. Alchian, *Corporate Management and Property Rights*, in MANNE, *supra* note 11, at 337, 343-44.

tion. While they do not directly share in the profits of an enterprise, successful performance increases the demand for their services as managers. Managers have a further incentive to maximize profit if their compensation is in some way linked to performance—stock options are a common example of this type of arrangement. Intensity of competition in the firm's product market also provides an incentive for managerial efficiency.[28]

The market for corporate control and the threat of cash tender offers in particular are of great importance in creating incentives for management to maximize the welfare of shareholders. Theoretically, shareholders may oust poor management on their own initiative, but the costs to individual shareholders of monitoring management performance and campaigning for its defeat in shareholder elections when performance is poor are prohibitive. On the other hand, inefficient performance by management is reflected in share price thus making the corporation a likely candidate for a takeover bid. Since a successful takeover bid often results in the displacement of current management, managers have a strong incentive to operate efficiently and keep share prices high.

III. The Williams Act

A. Disclosures by the Offeror

Section 13(d) of the Williams Act[29] provides that any person who obtains more than a five percent beneficial interest in a company must file with the SEC. Under rule 14D-1,[30] any person seeking to make a tender offer that will result in his becoming the owner of more than five percent of a class of equity securities must file a schedule 14D-1[31] statement with the SEC. Rule 14D-1 also requires that an offeror make extensive disclosures to the target company's shareholders. The information to be disclosed includes the name and background of the offeror (including any criminal convictions within the past five years), the highs and lows at which the target company's security has been traded in each quarter during the past two years, the offeror's source of funds, the offeror's financial condition, and any contracts or negotiations

28. It has been argued that conditions of monopoly in product markets lessen the constraints on management behavior. *See* Williamson, *Corporate Control and the Theory of the Firm*, in MANNE, *supra* note 11, at 281, 294-95. *But see* Jensen & Meckling, *supra* note 24, at 329-30.

29. 15 U.S.C. § 78m(d)(1) (Supp. V 1975), *as amended by* Pub. L. No. 95-213, § 202, 91 Stat. 1494 (1977).

30. 17 C.F.R. § 240.14d-1 (1977).

31. 17 C.F.R. § 240.14d-100 (1977).

within the past three years between the target and the offeror concerning a merger or takeover. The offeror must also disclose the purpose of the tender offer including any plan for a future merger, reorganization, liquidation, transfer of any material amount of the target's assets, or any intended change in the existing board of directors or management.[32] Moreover, section 14(e),[33] the general antifraud provision of the Act, has been interpreted to require disclosure of material information known to the offeror while the offer remains outstanding, even if such information was not otherwise required.[34] Some commentators have argued that such diverse items as financial statements of the offeror and the basis for setting the tender offer price are material and should be disclosed to investors.[35]

Proponents advance three major justifications for these disclosure requirements: (1) the need to give shareholders parity of information with the offeror; (2) the anomaly of disclosure requirements in other control-transfer situations such as the exchange offer and proxy contest but not the cash tender offer; and (3) protection of the corporation against corporate raiders. These justifications will now be separately evaluated.

1. Placing shareholders on an equal footing with offerors.—One of the leading supporters of the Williams Act has argued in a famous article[36] that disclosures by the offeror are necessary "if public investors are to stand on an equal footing with the acquiring person in assessing the future of the company and the value of its shares."[37] The legislative history of the Act also reflects this concern.[38]

The argument has a surface plausibility. Shareholders faced with a tender offer must decide whether to tender their shares. If they decide to sell, they will no longer have any interest in the company, and therefore information concerning the background and future plans of the offeror is irrelevant to them.[39] While shareholders who follow this

32. For a more comprehensive description of required disclosures by a tender offeror in schedule 14D-1, see Gould & Jacobs, *The Practical Effects of State Tender Offer Legislation*, 23 N.Y.L. SCH. L. REV. 399, 410 n.36 (1978).

33. 15 U.S.C. § 78n(e) (1970).

34. *See, e.g.*, Sonesta Int'l Hotels Corp. v. Wellington Assocs., 483 F.2d 247, 250 (2d Cir. 1973).

35. *E.g.*, Haft, *Disclosure In Cash Tender Offers*, 8 REV. SEC. REG. 975 (No. 3 1975).

36. Cohen, *A Note on Takeover Bids and Corporate Purchases of Stock*, 22 BUS. LAW. 149 (1966).

37. *Id.* at 150.

38. *E.g.*, H.R. REP. No. 1711, 90th Cong., 2d Sess. 3, *reprinted in* [1968] U.S. CODE CONG. & AD. NEWS 2811.

39. A shareholder who has decided to disinvest may nevertheless remain an involuntary in-

course receive a premium above market, they relinquish the right to participate in growth of the company under new management if the tender offer is successful. Some shareholders, perhaps those who believe that the offeror would not pay a premium for control unless it thought it could turn the target around, may prefer not to tender their shares in order to retain an equity participation after the takeover. Of course, this strategy requires that not too many shareholders follow it because the success of the tender offer depends on a sufficient number of shares being tendered. The risk that the tender offer will fail if not enough shares are tendered imposes a cost on the shareholder who refuses to tender in hopes of participating in the company under new management. If the tender offer is defeated, shareholders who refused to sell lose the premium they could have received had they tendered. Thus, shareholders must balance the cost of not tendering—the lost premium of the tender offer price above market—against expected gains under new management. While shareholders can readily ascertain the cost of not tendering by simply multiplying the premium by the number of shares they own, the expected gains under new management are speculative. The rational shareholder in making a decision whether to tender may well desire such information as the basis for setting the offer price and any future plans of the offeror.[40] Nevertheless, it is doubtful that the offeror should be required to provide this information.

A duty of disclosure is not imposed in all securities transactions.[41] Generally, the securities laws impose an affirmative duty of disclosure only on persons who owe some fiduciary duty to the affected party. As the SEC stated in *Cady, Roberts & Co.*, the seminal case on insider trading:

> Analytically, the obligation [to disclose material, nonpublic information prior to trading] rests on two principal elements; first, the existence of a relationship giving access, directly or indirectly, to

vestor in the target if the tender offer is oversubscribed and shares are only accepted on a pro rata basis. Even this risk can be eliminated, however, by selling in the market (although the premium offered by the offeror may not be available).

40. An example posed by then Chairman Cohen in the Senate Hearings illustrates this dilemma. Chairman Cohen posits a situation in which a company's stock is selling for $5 a share but has a liquidation value of $15 per share. A tender offeror then offers $6 per share. Chairman Cohen suggests that shareholders cannot make an intelligent decision whether to tender unless they are informed of the liquidation value of their shares. Once informed, they may well believe that the $6 offer price is inadequate. *See Hearings on S. 510 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. 18 (1967) (testimony of Chairman Cohen).

41. *See generally* Fleischer, Mundheim, & Murphy, *An Initial Inquiry Into the Responsibility to Disclose Market Information*, 121 U. PA. L. REV. 798 (1973).

information intended to be available only for a corporate purpose and not for the personal benefit of anyone, and second, the inherent unfairness involved where a party takes advantage of such information knowing it is unavailable to those with whom he is dealing.[42]

The typical tender offer situation, however, involves neither of these two rationales for the duty of disclosure. The offeror is usually an outsider with no special relationship to the target and no access to inside information. In this situation, prior to passage of the Williams Act, the offeror had no duty to disclose.[43]

In *Mills v. Sarjem Corp.*,[44] for example, an offeror purchased eighty percent of the shares of a target company that owned bridges. The offeror at the time of the tender offer planned to sell the bridges to a municipal authority in exchange for revenue bonds at a substantial profit. A shareholder then brought an action under rule 10b-5 alleging that the offeror had a duty to disclose its plans to sell the bridges if the tender offer was successful. Rejecting this contention, the court focused on the absence of any special relationship between the offeror and the target:

> There seems to be no question but that the sellers and purchasers of the shares of stock dealt at arm's length, aud that the selling shareholders were plainly on notice of the fact that the purchasing syndicate designed to obtain all of the capital stock of the corporation. Surely plaintiffs must have anticipated the likelihood that the defeudants had a profit-making purpose in mind, especially when the price per share offered to them was substantially higher than the market value of the shares. The entire field of securities transactions is to some degree speculative in nature, and sales are usually motivated by a difference in opinion between vendor and purchaser regarding the future prospects of the particular security involved. Such was clearly the case here, and in the absence of any fiduciary duty it was not incumbent upon the defendants to divulge their plans with respect to a subsequent resale of the property.[45]

Mills and the Williams Act take opposite approaches to the issue whether a third party, absent a special or fiduciary relationship, has an obligation to disclose admittedly material information to shareholders. To decide which represents the preferable approach requires an understanding of the economics of information production.

42. Cady, Roberts & Co., 40 S.E.C. 907, 912 (1961) (footnote omitted).

43. *See generally* Fleischer & Mundheim, *Corporate Acquisition By Tender Offer*, 115 U. PA. L. REV. 317, 328-35 (1967).

44. 133 F. Supp. 753 (D.N.J. 1955).

45. *Id.* at 764.

For the market for corporate control to function effectively, outsiders must have adequate incentives to produce information.[46] Outsiders are not generally privy to inside information about a potential target. A decision to tender only occurs after an offeror determines that the target will be more profitable in its control and that a tender offer is likely to succeed. These decisions involve research costs. The incentive to produce this information is the expected gain from the appreciation of the offeror's equity investment after obtaining control. Any legal constraint that limits the ability of owners of privately produced information to realize its exchange value will discourage devoting resources to produce new information. In other words, a failure to recognize a property right in privately produced information will decrease the incentives to produce this information.[47]

Recognition of a property right in information—a right or entitlement to invoke the coercive machinery of the state to exclude others from its use—is not unusual in the American legal system. The granting of a patent is a familiar example of a legally enforceable property right. Another way in which the legal system can grant a property right in information is by allowing a party who possesses valuable information to enter into and enforce contracts without having to disclose the information to the other party.[48] Imposing a duty of disclosure is tantamount to requiring that the benefit of the information be publicly shared. This requirement of disclosure is antithetical to the basic notion of a property right, which by definition entails the legal protection of private appropriation for private benefit.[49]

The disclosure requirements of the Williams Act—justified by a goal of ensuring parity of information between the offeror and shareholders—dilute the value of the property right in privately produced information. Provisions like the filing requirements and requirements of disclosure of identity and source of funds increase the cost of a tender offer and thereby diminish takeover incentives. Other provisions such as the requirement of disclosure of intentions have a more serious impact. This requirement is perhaps the most objectionable feature of the Williams Act. The securities laws generally impose no

46. *See* Manne, *Cash Tender Offers For Shares—A Reply to Chairman Cohen*, 1967 DUKE L.J. 231, 236.

47. Manning, *Discussion & Comments On Papers By Professor Demsetz and Professor Benston*, in MANNE, *supra* note 11, at 109.

48. Kronman, *Mistake, Disclosure, Information, and the Law of Contracts*, 7 J. LEGAL STUD. 1, 15 (1978).

49. *Id.*

corresponding requirement on incumbent management.[50] If management and another party agree to a merger, for example, there is no duty to disclose until the agreement is closed. It is highly unlikely that an outsider will know with any certainty what his future plans are. The premature and tentative nature of any outsider's plans create great uncertainty over when such disclosure is required.[51] This uncertainty has resulted in considerable litigation. Indeed, a favored defensive tactic of management to frustrate a tender offer is to charge that an offeror has violated the Williams Act by not disclosing its intentions. The cost of uncertainty is a deterrent to tender offers. More fundamentally, disclosure of intentions forces an offeror to share information that he has used resources to produce, without receiving any compensation in return. In other securities transactions, inequalities of bargaining power attributable to superior intelligence, research, or diligence are not only permitted but are considered to be integral to a free market economy.[52] The law does not require a purchaser of stock in an exchange or over-the-counter market to inform a seller why he believes the value of stock is or will be greater than the purchase price despite the fact this information would be extremely useful to the seller. Yet a tender offeror who believes that a company would be more profitable if managed in a different way, merged, or even liquidated must, under the Williams Act, disclose his intentions. There is no sound reason why investors should stand on an "equal footing" in the latter situation but not the former. A proponent may defend the duty of disclosure for insiders on the grounds that insiders are likely to acquire information, not by superior efforts, but by virtue of their superior access.[53] Thus, a rule requiring insiders to disclose does not significantly deter the production of new information.[54] But this justification is inapplicable to the typical tender offeror, and the Williams Act, by imposing on outsiders a quasi-fiduciary duty of disclosure instead of recognizing a property right in privately produced information, greatly reduces the incentive to undertake a takeover attempt.[55]

50. *But see* note 104 *infra.*

51. Incumbent management, which is in a much better position than an outsider to be aware of its future plans, is under no corresponding disclosure obligation. *See* Manne, *supra* note 46, at 250.

52. Brudney, *A Note On Chilling Tender Solicitations*, 21 RUTGERS L. REV. 609, 615 (1967).

53. As Professor Posner has stated, "Insider trading does not reward efficient managemeut as such. It rewards the possession of confidential information, whethcr it is favorable or unfavorable to the corporation's prospects." *See* R. POSNER, *supra* note 23, at 308.

54. Prohibitions on insider trading do, however, cause some market inefficiency by preveuting share prices from reflecting all available information.

55. The distinction in securities law between circumstances in which corporate insiders and tender offerors, as parties to negotiations with shareholders for the possible sale of securities, have

The goal of ensuring parity of information between offerors and shareholders at the expense of recognizing a property right in privately produced information is also evident in several recent proposals. One commentator[56] has argued that section 14(e) of the Williams Act, the general antifraud section, requires that the offeror disclose "all financial and business information relating to the target that it has obtained at any time prior to the making of the offer" even if he obtained this information "solely from publicly available materials of the target." Moreover, this commentator urges, the offeror should also be required to disclose its basis for setting the tender price: "[S]uch disclosure would elicit a great deal of information about (1) the 'hidden values' that the target may possess, of which the ordinary target shareholder may not be aware, and (2) the special values the target has in the offeror's hands."[57] It is difficult to conceive of proposals that would have a more devastating impact on the incentives of an offeror to devote resources to produce new information. Adoption of these proposals would effectively cripple the market for corporate control by substantially impairing the ability of the offeror to realize the exchange value of privately produced information.

2. *The "gap in federal securities law" argument.*—A second argument in justification of the disclosure requirements of the Williams Act is that disclosure is already required in other takeover devices such as the proxy contest and the exchange offer.[58] The argument overlooks the fact that other methods of acquiring control that appear to be closely related to a tender offer, such as a market purchase from a controlling shareholder, are not regulated.

Although various takeover devices share the common objective of obtaining control, the purposes of disclosure in each of them are not identical. In a cash tender offer or a proxy contest, for example, insurgents are attempting to displace incumbent management. Yet the two are fundamentally different. In a proxy contest, the parties compete for the right to manage somebody else's money; in a cash tender offer, by

a duty to disclose information relevant to the shareholders' decisions and circumstances in which there is no duty of disclosure plays a similar role to the distinction in contract law between circumstances in which a seller of goods has a duty to disclose defects in the goods and circumstances in which there is no duty of disclosure. In a recent article, Professor Kronman has argued that cases involving contracts impose a duty of disclosure with respect to information the seller might casually acquire and not with respect to information the seller could acquire only after a deliberate search. *See* Kronman, *supra* note 48. In the tender offer context, insiders typically acquire information casually while offerors only do so after a deliberate search.

56. Haft, *supra* note 35.

57. *Id.* at 981.

58. *See, e.g.*, H.R. REP., *supra* note 38, at 3.

contrast, an outsider tries to acquire the right to dictate management policy by virtue of his own ownership. It would not be illogical to have a system in which a party striving to manage a corporation as the representative of shareholders must make certain disclosures while a party who wishes to nominate management as a result of majority ownership or at least working control is free not to disclose.

Nor do disclosures required in exchange offers present a compelling case for disclosures in the cash tender offer context. With respect to exchange offers in which the stock offered in exchange for shares tendered must be registered under the Securities Act of 1933, SEC regulations demand that the registration statement filed in connection with the exchange disclose similar information about both the offeror and offeree companies.[59] The theory is that the shareholder must have adequate information about both companies to make an intelligent decision whether to accept the offered exchange.[60] The desirability of this twofold disclosure requirement, however, is debatable. The rational shareholder's decision whether to accept the exchange offer will rest on two factors: (1) the proper valuation of his shares under current management, and (2) the value of the exchange package securities. Disclosure by the offeror of information about the target company under current management can only mislead the shareholder/offeree with respect to (1) by placing disproportionate emphasis on aspects of current target company performance that are already correctly weighed and reflected in the market price of traded shares. If the exchange package securities are already publicly traded, the same consideration applies to them, so that the best information about (2) is also available without disclosure. If the eventual success of the offeror's management of the target company will determine the ultimate value of the exchange package securities, the rational shareholder may need more information than market prices afford in order to make his decision, but current disclosure requirements answer this need indirectly at best.

Even if it is assumed that disclosure in exchange offers is useful, it does not follow that disclosure is appropriate in a cash tender offer. Unlike the shareholder in an exchange offer who is solicited to be both a buyer and a seller (a seller of his shares in the offeree company and a buyer in the offeror company), a shareholder in a cash tender offer can only become a seller. Thus, while the shareholder in a successful exchange offer maintains a continuing investment, many shareholders in a successful cash tender offer disinvest and have no further interest in

59. Form S-1, General Instruction F, Items 6-10, 12.
60. Fleischer & Mundheim, *supra* note 43, at 348.

either the offeror or target company. For these shareholders who receive cash for their shares, any disclosure is irrelevant.[61] Shareholders who refuse a cash tender offer may do so either in order to participate in the benefits of the company under new management or in order to defeat the tender offer. These two goals are remarkably like the *only* ones available to shareholders in the exchange offer context. Unlike the exchange offer, the cash tender offer does not succeed or fail according to which of these goals shareholders find more attractive. Thus, even if exchange offer disclosure requirements do ensure that shareholders receive otherwise unavailable information relevant to their decisions, the same disclosure requirements may bear no relation to the decisions of cash tender offerees.

3. The protection against corporate raiders rationale.—In commenting on an earlier version of the Williams Act, Senator Harrison Williams stated:

> 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 . . . .
>
> The ultimate responsibility for preventing this kind of industrial sabotage lies with the management and the shareholders of the corporation that is so threatened. But the leniency of our laws places management and shareholders at a distinct disadvantage in coming to grips with the enemy.[62]

Although the Williams Act as enacted explicitly disavowed any desire to discourage tender offers,[63] fear of corporate raiders is nevertheless a theme in the legislative history.[64]

The theme has two components.[65] The first is an assumption that "proud old companies" that have been operating profitably for years may somehow be turned into "corporate shells" by unscrupulous "white-collar pirates." There is no empirical support for this suspicion. Indeed, the existing evidence is precisely to the contrary. The "proud old companies" that have been targets in cash takeovers have generally not performed well.[66] The second assumption is that outsiders who

61. The shareholder who cashes out tends to receive the present value of his shares under efficient capital market theory. Equitable considerations would also seem satisfied, since the premium paid exceeds the preseut value of the shares.

62. 111 CONG. REC. 8257-58 (Oct. 22, 1965).

63. *See, e.g.*, H.R. REP., *supra* note 38, at 4.

64. *See, e.g., Hearings, supra* note 40, at 43 (remarks of Sen. Kuchel).

65. *See generally* Taussig & Hayes, *supra* note 19.

66. *See* notes 9-10 *supra* & accompanying text.

buy control of a company, liquidate all or some of its assets, and then, in Senator Williams' words, "split up most of the loot among themselves," are evil or unethical. While it is understandable that incumbent management who have a vested interest in maintaining their positions could have this view, it has no empirical support and is contrary to economic theory. Empirical evidence suggests that only a small percentage of tender offers are made for the purpose of liquidating the assets of the target.[67] Moreover, tender offers that are made for this purpose should not necessarily be discouraged. If the liquidation value of an enterprise is greater than its going concern value, the tender offeror renders an economic benefit by liquidating its assets. As long as the tender offeror does not take more than its pro rata share of the liquidation value, all shareholders benefit by liquidation.

Even if it is conceded that corporate raiders pose a real danger, it is still questionable whether the Williams Act is the right solution. Once a tender offeror gains control, fiduciary duties under state law preclude looting or other appropriation of corporate assets. While legal constraints against looting may not be totally effective against deterring such conduct, it is not clear how much incremental deterrent effect prophylactic disclosure requirements of identity and background have on unscrupulous offerors. Moreover, whatever deterrent effect on looters these disclosure requirements have must be balanced against the deterrent effect of disclosure requirements on bona fide tender offers that benefit all shareholders. Because there is no evidence to suggest that a significant number of tender offerors are looters, the benefits of increased protection that disclosure requirements provide against potential raiders is outweighed by the costs of their perpetuation of inefficient management.

B. Other Obligations of the Offeror Under the Williams Act

The Williams Act also contains several provisions designed to prevent hasty, ill-considered decisions by shareholders of the target corporation and to ensure that they receive equal treatment. Section 14(d)(5)[68] of the Act provides that shareholders must have the right to withdraw shares tendered within seven days of the time the tender offer is first published.[69] Section 14(d)(6)[70] requires the pro rata acceptance

67. Taussig & Hayes, *supra* note 19, at 110.
68. 15 U.S.C. § 78n(d)(5) (1970).
69. Offerors must also grant shareholders the right to withdraw shares tendered after the expiration of 60 days from the date of the original offer if the tendered shares have not yet been paid for by the offeror.
70. 15 U.S.C. § 78n(d)(6) (1970).

of securities tendered within ten days of a tender offer for less than all of the outstanding shares of a class of stock of a target company. Section 14(d)(7)[71] entitles all shareholders to any increase in price in the original offer. Thus, if the offeror increases the consideration to be paid for tendered securities during the course of the offer, it must also pay the increased price to security holders who tendered at a lower price before the announcement of the increase, regardless of whether the securities previously tendered were actually purchased before or after the announcement.

All these provisions increase the cost of conducting a tender offer. Section 14(d)(7), which requires an offeror to pay any increase in the tender offer price to all shareholders, is by far the least justifiable of the nondisclosure requirements of the Williams Act. Enacted to "assure fair treatment of those persons who tender their shares at the beginning of the tender period, and to assure equality of treatment among all shareholders who tender their shares,"[72] section 14(d)(7) imposes a duty on offerors that would not otherwise be implied. In certain situations, because of a fiduciary relationship, the Act imposes a duty to deal fairly and equally with all shareholders. Directors, for example, cannot selectively declare a dividend payable to some shareholders but not to others of the same class. It is highly doubtful, however, whether it is appropriate to impose this duty of equal treatment in the tender offer context. In other instances of market purchase of shares, no similar duty is imposed. If a purchaser accumulates a large block of stock in the open market, nobody could seriously contend that all sellers are entitled to the highest price paid by the purchaser to any seller.

A tender offeror may decide to increase the price offered after it becomes clear that the initial price was insufficient to attract the desired number of shares. This procedure is perfectly compatible with a free market economy in which sellers value their securities differently and, therefore, every increment in price will attract more willing sellers. Section 14(d)(7) forces an offeror to pay to all shareholders the highest price that any shareholder demands in order to attain the desired number of shares even though many shareholders would have sold for far less.[73] The result is to increase greatly the cost of a tender offer.

71. 15 U.S.C. § 78n(d)(7) (1970).

72. H.R. REP., *supra* note 38, at 11.

73. Rule 10b-13, 17 C.F.R. § 240.10b-13 (1978), embodies a similar philosophy of equal treatment of shareholders. The rule prohibits an offeror from purchasing securities that are the subject of a tender offer on terms other than those of the tender offer regardless of whether shareholders are willing to sell. This rule can affect an offeror adversely, particularly if a third party is competing with the offeror for target shares. In some cases, offerors have been precluded by rule

The withdrawal and pro rata provisions also impose additional costs. Section 14(d)(5), by giving shareholders an unconditional right to withdraw during the first seven days of a tender offer, essentially allows shareholders a put without any return compensation. If the market price does not rise above the tender price, a shareholder will have no reason to withdraw his tender. But if the market price rises above the tender price or if a competing offer develops at a higher price, the shareholder can withdraw. The withdrawal provisions can result in an inadequate number of shares being tendered and thus force the tender offeror to increase the tender price even though an adequate number were originally deposited.

The pro rata provisions embodied in section 14(d)(6) give shareholders an incentive to adopt a "wait and see" attitude during the first ten days of a tender offer. If tender offerors could purchase on a first-come-first-serve basis, shareholders would have a much greater incentive to tender early. This delay in tendering decreases the likelihood of a successful tender offer by providing management with an opportunity to marshal its resources and engage in a variety of defensive tactics to frustrate the tender offer.

It may be argued, however, that the withdrawal and pro rata provisions benefit shareholders by providing them with additional time to respond to a tender offer. During this additional time, competing offers may be made at a higher price than the original tender offer. Whether shareholders benefit more under a system most favorable to the original offeror—one with no withdrawal or pro rata provisions—or under a system in which the presence of these provisions encourages competing bids is an empirical question not subject to an armchair resolution. However, it should be noted that competing offers would develop even if tender offers were unregulated. Presumably, shareholders faced with a tender offer are not totally ignorant of the possibility of a competing offer and therefore will not rush to tender their shares immediately. Even if the shareholders themselves are not aware of a competing offer, it is in the interest of parties interested in making a competing offer to make their intentions known as soon as possible after the original tender offer.

10b-13 from purchasing shares at a price higher than the tender offer price to match the price being offered in open market purchases by a third party. *See* Einhorn & Blackburn, *The Developing Concept of "Tender Offer": An Analysis of the Judicial and Administrative Interpretations of the Term*, 23 N.Y.L. SCH. L. REV. 379, 393 (1978).

C. The Types of Transactions That Are Governed By the Williams Act

A tender offer is generally understood to be a public invitation to all shareholders of a corporation to tender their shares at a specified price. The Williams Act, however, nowhere defines "tender offer." As a general rule, courts have refused to extend the Williams Act requirements to market transactions that do not fit the paradigm of the conventional tender offer.[74] Several commentators,[75] however, have argued that a greater range of transactions should be regulated by the Williams Act. One commentator, for example, has advocated that the Williams Act should apply to all purchases "found capable of exerting the same sort of pressure on shareholders to make uninformed, ill-considered decisions to sell which Congress found the conventional tender offer was capable of exerting."[76] To determine whether a transaction should be regulated as a tender offer, the author suggests that courts examine "the shareholder impact of particular methods of securities acquisition."[77] Such elements as time limits, premium prices, or specification of the number of shares to be purchased would indicate that the shareholder impact of the offer is comparable to that of a conventional tender offer.

This proposed shareholder impact test, however, is fraught with uncertainty and therefore would further hamper the operation of the market for corporate control. Under the shareholder impact test, an offeror does not know in advance whether an offer will be subject to Williams Act regulations. Thus an offeror cannot be sure whether it is under a duty to disclose and whether the offer is subject to the matching price, withdrawal, and pro rata provisions of the Williams Act. This uncertainty inevitably has a chilling effect on attempts to gain control.

More fundamentally, it is not clear precisely what evils would be redressed by expanding the definition of tender offer. A third party's offer to purchase securities, even if qualified by a time limit or accompanied by publicity, does not force shareholders to make uninformed, ill-considered decisions any more than the typical market transaction.

74. *See generally id.*

75. *See, e.g.*, Moylan, *Exploring the Tender Offer Provisions of the Federal Securities Laws*, 43 GEO. WASH. L. REV. 551 (1975); Note, *The Developing Meaning of "Tender Offer" Under the Securities Exchange Act of 1934*, 86 HARV. L. REV. 1250 (1973).

76. *See* Note, *supra* note 75, at 1275.

77. *Id.*

Only under the most paternalistic view of the securities markets should all forms of market transactions be regulated to protect shareholders.

Other commentators have argued that pre-tender offer purchases of securities by an offeror should be subject to Williams Act requirements.[78] An offeror frequently purchases shares in the open market or in privately negotiated transactions before making a formal tender offer. Shareholders who sell during this period are not entitled under present law to Williams Act protections. Nevertheless, it has been suggested that pre-tender offer purchases should be regulated as tender offers to prevent the offeror from getting a free ride at the expense of early purchasers. Similarly, some commentators[79] have urged that an offeror should not be permitted to purchase shares in the market after a tender offer has terminated. The concern appears to be that the offeror should not be allowed to take advantage of unsettled conditions after a tender offer and purchase shares below the tender price. Responding to this concern, the SEC has proposed a rule that would require that purchases made by an offeror within forty days after termination of an offer be integrated with the original tender offer.[80]

The suggestions that pre- and post-tender offer purchases of securities by an offeror be regulated as tender offers represent a considerable extension of the Williams Act's policy of equality of treatment among shareholders. There is simply no reason why, in a free market economy, all shareholders must be treated equally in this respect. Offerors should be allowed to contract freely with shareholders for the sale of their shares at prices and terms satisfactory to the parties. Moreover, like the Williams Act itself, these proposals focus on the treatment of target shareholders without adequately considering the effect on the offeror. Each extension of the Williams Act lessens the offerors' incentive to try for control. In sum, the adverse effects of the Williams Act on the market for corporate control should not be increased by regulating pre- and post-tender offer purchases of securities as tender offers.

D. *Regulation of Disclosures by Management*

Pursuant to its rulemaking powers, the Commission has promulgated rule 14d-4,[81] which requires target management to file a schedule 14D statement if it recommends shareholders accept or reject a tender

78. *See, e.g.*, Lipton, *Book Review*, 72 MICH. L. REV. 358, 362-63 (1973).
79. *See, e.g.*, Black & Sparks, *Triggering the Williams Act*, 8 REV. SEC. REG. 967, 970 (1975).
80. Proposed Rule 14d-6(a), SEC Exchange Act Release No. 34-12676, 2 FED. SEC. L. REP. (CCH) ¶ 24,286A (Aug. 2, 1976).
81. 17 C.F.R. § 240.14d-4 (1977).

offer. The 14D statement, much of which must be summarized in any communication sent to shareholders, requires management to disclose its reasons for the recommendation. Moreover, any management recommendation or other disclosure is subject to the anti-fraud rules of section 14(e).

These regulations of management recommendations conceivably could serve a salutary function by deterring unsubstantiated claims by management calculated to frustrate a tender offer, although enforcement of fiduciary duties under state law could also perform this function. Unfortunately, judicial interpretation has somewhat limited the utility of these provisions of the Act. In *Gulf & Western Industries, Inc. v. Great A. & P. Tea Co.*,[82] for example, target management was alleged to have violated section 14(e) by urging shareholders to reject a tender offer because the price was too low, without disclosing any basis for this conclusion. An efficient capital market makes it highly unlikely that the market price of the target shares is too low. Thus, a tender offer price above market price will rarely be inadequate, and a statement to the contrary by management without any basis would seem to be a misleading statement within the meaning of section 14(e). Nevertheless, the court held that the statement was not unlawful, emphasizing that the "term 'inadequate' when used in connection with the price of a stock is a highly subjective one," and that stock prices are determined by "the whims and caprice of the crowd"[83] as well as by objective criteria. The target management statements involved in *Gulf & Western* are precisely the type of recommendations which should be prohibited by section 14(e).

The efficacy of Williams Act regulation of management disclosures has been further weakened by the Supreme Court's recent decision in *Piper v. Chris-Craft Industries, Inc.*[84] Holding that a defeated tender offeror had no implied right of action under section 14(e) to sue target management or a competing offeror for damages, the court reasoned that because the Act was intended to protect ordinary shareholders, tender offerors should not be allowed an implied right of action even if they held stock in the target company. The problem with this reasoning, however, is that an offeror has both superior access to information about section 14(e) violations by management and greater incentives to discover them than does a shareholder. *Chris-Craft* will reduce significantly section 14(e)'s deterrence of management misrep-

82. 356 F. Supp. 1066 (S.D.N.Y.), *aff'd*, 476 F.2d 687 (2d Cir. 1973).
83. *Id.* at 1071.
84. 430 U.S. 1 (1977).

resentations.[85]

E. Whether the Williams Act Should Be Amended to Impose an Affirmative Duty of Disclosure on Management

The Williams Act does not impose any affirmative disclosure obligation on a management team confronted by a tender offer. Commentators are almost unanimous in urging that such an affirmative duty should exist.[86] Aside from the uncritical advocacy of many for more disclosure, it is unclear what benefit would flow from an affirmative duty of disclosure by management.

Presumably, disclosure is mandatory because management is in the best position to possess information about the target company that is relevant to shareholders in deciding whether to tender. Such information could consist of an explanation of disappointing operating performance or a future plan to generate increased earnings. While management undoubtedly has superior access to this type of information, it does not follow that management should have an affirmative disclosure obligation. Under efficient capital market theory, much of this information is reflected in the market price of the target's securities. Thus, shareholders need information concerning the target only if this information is not already reflected in the market price of the target's securities. It is conceivable that management will possess inside information not reflected in security prices primarily because of prohibitions against insider trading. Efficient capital market theory, however, suggests that this situation is relatively rare. Moreover, any gains from disclosure of inside information that would otherwise not be made public absent an affirmative disclosure obligation do not outweigh the harm to shareholders that wonld result from self-serving disclosures of management designed to defeat a tender offer.

F. The Williams Act: An Appraisal

The legislative history of the Williams Act[87] and leading cases[88] unequivocally state that the Act was intended to protect shareholders.

85. It is not clear that *Chris-Craft* will prevent tender offerors from quietly inducing friendly shareholders of the target company from bringing suit on section 14(e) violations and others so as to accomplish the same ends as a suit by the tender offer. *See* 430 U.S. at 42 n.28.

86. *E.g.*, Krasik, *Tender Offers: The Target Company's Duty of Disclosure*, 25 BUS. LAW. 455 (1970); Note, *A Proposal for Affirmative Disclosure By Target Managemcnt During Tender Offers*, 75 COLUM. L. REV. 190 (1975).

87. *See, e.g.*, note 38 *supra*.

88. *E.g.*, Piper v. Chris-Craft Indnstries, Inc., 430 U.S. 1 (1977); Rondeau v. Mosinee Paper Corp., 422 U.S. 49 (1975).

Whether the Williams Act achieves this result, however, is far from obvious. The greatest risk for a shareholder facing a tender offer is that he will sell his shares for an inadequate price. The term "inadequate," however, has two distinct meanings in this context. First, the tender price is inadequate if it is less than the intrinsic value of the shares at the time of sale. Presumably, management exhortations that the tender price is inadequate and that the offeror is trying to gain control at "bargain basement" prices have this type of situation in mind. Second, a tender price could be inadequate if the shareholder could somehow receive a still higher price even though the tender price exceeds the value of the target securities. This situation could occur, for example, if the value of the target securities would appreciate under new management, if the tender offeror increased the tender price, or if a competing tender offer developed.

The Williams Act tender offer provisions are not primarily concerned with inadequacy of price in the first sense. The required disclosures by the offeror relate to the offeror and its future plans, not to relevant information about the target. Management, which is in the best position to appraise whether the market price of the target's shares approximates their intrinsic value, is under no duty to disclose. Moreover, as should now be clear, in an efficient capital market at equilibrium there is little danger that shareholders will get less than their shares are worth if they receive a premium above market.

Much of the Williams Act, therefore, is designed to prevent shareholders from receiving an inadequate price in the second sense. Disclosure of the offeror's future plans may alert the shareholder that his shares will be worth more under new management; the requirement that the offeror retroactively grant any increase in price to all shareholders ensures that shareholders who tender early will not be prejudiced; the pro rata provisions protect shareholders who wait on the sidelines for a counter-offer against the risk that the offeror will satisfy its needs from other willing shareholders. On their face, these provisions purport to protect shareholders. Two questions nevertheless remain—whether protection of shareholders in this manner is an appropriate goal of securities regulation, and whether the costs imposed by this type of regulation outweigh other benefits to shareholders in an unregulated market.

The securities laws generally impose a duty of disclosure and fair dealing on insiders or other parties with access to inside information. But the securities laws have never been interpreted to mandate full disclosure and egalitarianism in all market transactions. In a typical securities transaction, a buyer does not have to disclose why he thinks the stock is worth more than his offer price, pay all sellers the same for their shares if some are willing to sell for less than others, or give all shareholders an equal opportunity to sell. Yet these are the requirements imposed on a tender offeror by the Williams Act. The Act stands alone among major pieces of securities regulation in imposing a quasi-fiduciary duty on a buyer in a securities transaction absent any fiduciary or special relationship.

Even if the Williams Act conformed with the goals of securities regulation, there remains the question whether the costs generated by the Act outweigh any benefit to shareholders. The existence of a takeover device such as the cash tender offer provides a mechanism for shifting control to those who can manage assets more effectively. The possibility that control could change hands gives incumbent management an incentive to perform efficiently and keep stock prices high in the interest of all shareholders. By increasing the cost of making a tender offer and by reducing the exchange value of privately produced information, the Williams Act limits the effectiveness of cash tender offers and thereby undermines a check against entrenched inefficient management to the detriment of current shareholders.

IV. State Takeover Statutes

A. *State Statutory Provisions*[89]

State tender offer statutes regulate tender offers when a target corporation has certain contacts with the state. Whether a target corporation is protected typically depends on such factors as (1) incorporation within the state, (2) principal place of business in the state, (3) substantial assets in the state, and (4) percentage of the corporation's total employees within the state.[90] In some states offerors who acquire more than a specified percentage of a class of stock of a target company and then intend to make a tender offer must file a form similar to a registration statement with both the state securities commission and the target within some prescribed period between ten and sixty days prior to the effective date of the offer.[91] Many states also require public disclosure at the time of the filing.[92] Disclosures under state statutes are usually

89. This subsection is based primarily on E. ARANOW, H. EINHORN, & G. BERLSTEIN, *supra* note 3, at 207-17.
90. *Id.* at 208.
91. Thirty states regulate tender offers in this manner. *Id.* at 212 & nn.44-46.
92. *Id.* at 212 & n.43.

considerably more extensive than under the Williams Act.[93] State tender offer statutes also usually provide a minimum period during which an offer must remain open and a period during which shareholders can withdraw any tendered shares. Most also contain pro rata purchase provisions in the event the tender offer price is increased. Finally, some states monitor the terms of an offer by requiring that it be "fair and equitable."[94]

To enforce compliance, virtually all state tender offer statutes provide that a hearing concerning the tender offer must be held if requested by the state securities commission or, in several states, by the target company. The purpose of the hearing is to determine whether the state statute has been complied with. If a tender offer does not comply with the state statute, the commissioner can usually sue in state court to enjoin the offer. Most state statutes also make an offeror liable in damages and even criminally liable for violations.

B. Effect of State Tender Offer Statutes

Like the Williams Act, state tender offer statutes are ostensibly intended to protect shareholders. It is difficult, however, to perceive how shareholders could benefit from them. State tender offer statutes share many of the shortcomings of the Williams Act. Disclosure provisions, typically more burdensome than corresponding provisions under the Williams Act, significantly increase the cost of using the tender offer and decrease the incentive to produce information. Expanded disclosure requirements under state law also provide target management with increased opportunities to embroil offerors in protracted and expensive litigation that reduces the likelihood of a tender offer's success. Similarly, the withdrawal, pro rata, and matching price provisions of state statutes suffer from the same deficiences as comparable provisions of the Williams Act.

In one major respect, state tender offer statutes go far beyond the Williams Act in regulating offerors. In most states, the requirement of a filing by the offeror with the state securities commissioner and the target between ten and sixty days prior to the effective date of the offer eliminates the element of surprise so crucial for success. The possibility that the commissioner or the target may demand a hearing to determine whether the tender offer is in compliance with state law increases the likelihood of delay. The pre-offer filing and hearing provisions of

93. *Id.* at 212-13.
94. *Id.* at 213-16.

state statutes provide target management with advance warning of future offers and time to attempt to defeat the offer.[95]

During the period between the initial filing and the effective date of the offer, target management can actively lobby against the prospective offer and undertake various defensive tactics designed to frustrate the pending tender offer. During this period, however, the offeror is generally prohibited from communicating with shareholders. The inevitable result of the prefiling and hearing provision is to make it more difficult for a tender offer to succeed. Thus, state tender offer statutes, even more than the Williams Act, pose a powerful threat to the operation of the market for corporate control.[96]

C. *State Tender Offer Statutes and the Competition for Corporate Charters*

In an important article, Professor Ralph Winter has demonstrated the importance of the competition for corporate charters in protecting the interests of shareholders.[97] If a state corporation code allowed management to profit at the expense of shareholders or otherwise failed adequately to protect shareholders' investment interest, shares of corporations chartered in such states would trade at lower prices than shares of comparable companies in other states. Indeed, this result is inevitable in an efficient capital market. Corporations that trade at depressed prices are at a disadvantage in competing for debt and equity capital and become likely candidates for a tender offer bid. The possibility of this scenario gives management an incentive to incorporate in a state with a corporation statute that allows the corporation to compete effectively in the capital markets. To facilitate this result, "[s]tates

95. The impact of delay is particularly great on the arbitrageurs who are generally considered crucial to a successful tender offer. Arbitrageurs typically purchase shares in the open market after a tender offer is announced at less than the tender offer price. If the tender offer is successful, the arbitraguers profit by tendering their newly purchases shares at the higher tender price. The delay resulting from state tender offer statutes increases both the period during which the arbitrageurs must hold shares and the risk that the tender offer might be enjoined or otherwise fail. The likely result is that arbitrageurs will purchase fewer shares. *See* Gould & Jacobs, *supra* note 32, at 419.

96. Given their extraterritorial effect, it is possible that state tender offer statutes pose an unreasonable burden on interstate commerce and are therefore unconstitutional. Another possibility is that these statutes are preempted by the Williams Act. *See, e.g.*, E. ARANOW, H. EINHORN, & G. BERLSTEIN, *supra* note 3, at 225-32; Langevoort, *State Tender-Offer Legislation: Interests, Effects, and Political Competency*, 62 CORNELL L. REV. 213, 241-54 (1977). For a recent case declaring Idaho's tender offer statute preempted by the Williams Act, see Great Western United Corp. v. Kidwell, 577 F.2d 1256 (5th Cir. 1978), *cert. granted*, 47 U.S.L.W. 3450 (Jan. 9, 1979).

97. Winter, *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251 (1977).

seeking corporate charters will try to provide legal systems that optimize the shareholders-corporation relationship."[98]

Since state tender offer statutes make tender offers more difficult and thereby decrease managerial incentives to maximize earnings, a corporation with the requisite relationship to a state that has this kind of statute will find it more difficult to raise capital. Nevertheless, as Professor Winter demonstrates, competition for corporate charters does not necessarily guarantee that corporations gravitate to states without tender offer statutes, because these statutes adversely affect the market for corporate control.

The advantage to a corporation of incorporating in a state without a state tender offer statute is that the corporation will be a more attractive investment opportunity and therefore will be able to compete more effectively in the capital market. While it is usually in the interest of management to operate in a legal environment conducive to success in the capital market, state tender offer statutes present a special case. Shareholders benefit if the corporation is not subject to a state tender offer statute. Management, however, has a conflict of interest since the very factor that benefits shareholders—an unhampered market for corporate control—also makes it more likely that management will lose their jobs. Management may well view the danger of losing their jobs as greater than any danger that will result from being subject to a state tender offer statute. In this event, it will not try to avoid the reach of state tender offer statutes despite the detrimental effect of these statutes on shareholders.

The extraterritorial effect of state tender offer statutes also hampers the effectiveness of competition for corporate charters. For this competition to be effective, corporations must be able to incorporate in states that optimize management-shareholder relationships. But the importance of incorporation is greatly diluted because the operation of these tender offer statutes is not triggered only by incorporation. In many states, percentage of assets or employees within a state, principal place of business within a state, as well as place of incorporation determine whether a corporation has sufficient contacts with a state to activate its tender offer statute. Since a corporation may be subject to the tender offer statutes of several states even if incorporated in a state with no such statute, it is far more difficult for states to compete for corporate charters by not having tender offer statutes.

98. *Id.* at 256.

V. Defensive Tactics Employed By Incumbent Management

In addition to the deterrent effect of the Williams Act and state tender offer statutes, defensive tactics utilized by management make successful consummation of a tender offer difficult. Defensive tactics fall into two basic categories: preventive measures taken to make a target corporation less attractive to a potential offeror and remedial devices undertaken to defeat an offer after it is made.[99]

A. Preventive Defensive Tactics

The purpose of preventive defensive tactics is to make a target less attractive to potential offerors. One way of achieving this objective is to adopt contractual provisions that depend on the continuation of target management. Such provisions can provide, for example, that loans from creditors will mature or obligations to bondholders will be in default if control shifts. Obviously, these contractual obstacles discourage tender offers.

A second major preventive tactic is the enactment of defensive charter or bylaw amendments. These amendments may provide for staggered directorships or the elimination of cumulative voting. Other possibilities include provisions limiting the total number of directors or the authority of shareholders to remove directors before the expiration of their terms. A related type of defensive amendment requires that standby successor directors be elected at the same time as the regular directors and that any vacancies that develop be filled by the standby directors.

One of the most popular defensive charter amendments is the establishment of supermajority approval requirements for any proposed merger or sale of assets involving the target and an offeror. Typically, supermajority provisions provide that any merger involving the target and any corporation owning a certain percentage of target stock (usually five or ten percent) must be approved by eighty or eighty-five percent of all shareholders. Mergers or sales of assets not involving a corporation that owns the specified percentage of target stock are not subject to the supermajority requirements.

These defensive charter amendments seem repugnant to the most basic principles of corporate democracy. Provisions that make it difficult, if not impossible, for a successful offeror to remove directors and substitute its own nominees allow management to perpetuate itself in

99. *See* notes 90-94 *supra.*

office even when management has lost the support of shareholders.[100] Since successful offerors may wish to replace inefficient incumbent management with management of their own choosing to improve performance, these defensive charter provisions discourage tender offers. Supermajority requirements appear to be similarly reprehensible. Offerors will frequently attempt to gain control of a target before effectuating a merger because a merger requires approval by the board of directors. If target management opposes a merger, it can often only be accomplished if a tender offer is first attempted. If a small minority of shareholders can block a merger, the gains to be expected from a successful tender offer and the incentive to tender are reduced.[101]

Given the constraints that charter and bylaw amendments place on the ability of shareholders to sell their shares at a premium, why do shareholders vote for them? Theoretically, shares of a corporation that has adopted this kind of amendment should trade for less than shares of an identical corporation without them. One possible explanation for this apparent irrationality on the part of shareholders is transaction costs. If the decline in the value of a corporation's shares is miniscule and the transaction costs associated with wading through proxy materials high, shareholders may be unwilling to take the time to digest the proposals in proxy materials.[102] A second possible explanation for shareholders' approval of charter amendments is deficiencies in disclosure.[103] Management statements to shareholders in proxy materials to

100. E. ARANOW, H. EINHORN, & G. BERLSTEIN, *supra* note 3, at 195.

101. The establishment of fair price provisions in charter or bylaw amendments also decreases the incentive to tender. These provisions typically set a minimum price at which controlling shareholders may buy out or squeeze out minority shareholders. E. ARANOW, H. EINHORN, & G. BERLSTEIN, *supra* note 3, at 196. Like supermajority requirements, fair price provisions reduce the benefit to an offeror of a successful tender offer.

102. Under this theory, the large institutional investors are more likely to vote against defensive charter and bylaw amendments than smaller investors. While the decline in share price resulting from the adoption of defensive amendments has a greater effect on large investors with more shares, the costs associated with digesting proxy materials are equal for both types of investors. Thns, larger investors have a greater incentive to analyze proxy materials.

103. The "deficiencies in disclosure" explanation is not entirely persuasive. In an efficient capital market, investors should be able to recognize deficiencies in disclosure despite inadequate disclosure. Nevertheless, inadequate disclosure may mislead some investors, particularly if management has inside information of an imminent tender offer. In this event, management has inside information that would not necessarily be reflected in share prices, even in an efficient capital market, and that it should have a fiduciary duty to disclose. *See, e.g.*, United States Smelting, Refining & Mining Co. v. Clevite Corp. [1969-70 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 92,691 (N.D. Ohio 1968). *But see* A & K Railroad Materials v. Green Bay & W.R. Co., 437 F. Supp. 636 (E.D. Wis. 1977).

Requiring disclosure in this context has none of the disadvantages of the Williams Act disclosure requirements. Management, unlike an offeror, is an insider with a fiduciary duty to its shareholders. Moreover, management, unlike the offeror, will not typically have expended funds to develop information for which it should be entitled to a property right.

persuade them to approve defensive amendments typically emphasize the advantages of stable and continuous management and omit any mention of management's purpose to perpetuate itself in office. Incumbent management may also state that defensive amendments discourage outsiders from making surprise attempts to gain control to the corporation's disadvantage, and prevent outsiders from making fundamental corporate changes without approval by a high percentage of shareholders. Attempts by shareholders to challenge management disclosures under rule 14a-9, which forbids false or misleading statements or omissions of material facts, have generally been unsuccessful.[104]

Both the transaction costs and deficiencies in disclosure explanations assume that defensive charter or bylaw amendments do not benefit shareholders. An alteruative explanation, however, is that these amendments are somehow in the interests of shareholders. The interests are obvious if shareholders are connected in some way with the management group. Defensive charter amendments also allow shareholders, because of attachment to management for whatever reason, to provide management with what is tantamount to a long-term contract enforceable by specific performance.

B. Remedial Tactics

The pro rata purchase and matching price provisions of the Williams Act give shareholders an incentive to delay tendering their shares. The withdrawal provisions allow shareholders who have tendered an opportunity to reconsider. During the time when shareholders are considering whether to tender or withdraw, target management has an arsenal of defensive tactics at its disposal to attempt to defeat the offer. The efficacy of these defensive tactics is indicated by a recent

104. In Elgin Nat'l Indus., Inc. v. Chemetian Corp., 299 F. Supp. 367 (D. Del. 1969), for example, the court rejected a claim that the failure by management to disclose in a proxy solicitation that the effect of defensive amendments would be to entrench and perpetuate management's control violated rule 14a-9.

Rowland Cook, chief of the SEC's office of disclosure policy, recently announced, however, that the SEC staff will review proxy materials closely to make sure that management makes adequate disclosure of proposals designed to ward off takeover attempts.

> According to the staff, companies should disclose, among other things:
>
> —The reasons for the proposal. If management knows of specific takeover attempts, they should be disclosed. And if it isn't aware of any merger plans, it should explain why it is proposing the changes at that time.
>
> —Existing provisions that discourage takeovers and whether the new proposals are part of a series of proposals that would tend to insulate the company from an acquisition.
>
> —How the proposals would work.
>
> —Whether the board voted on the proposals. Consideration also should be given to including the reasons any directors dissented if the vote wasn't unanimous, the staff said.

Wall St. J., October 18, 1978, at 2, col. 3.

study that found that cash tender offers that were opposed by management had a success rate of only 26.7 percent while uncontested offers had a success rate of 89.2 percent.[105]

1. Shareholder communications. —One of the simplest and most commonly used defensive tactics by target management is direct communications to shareholders urging them not to tender. The basic thrust of such communications is that the long-run advantages to shareholders of not tendering exceeds any short-term gain realized from acceptance of the offer.[106] Management communications typically emphasize that any poor operating performance is temporary; that management anticipates increased sales and profits; that the tender offer price is inadequate and an attempt to gain control of the target at "bargain basement" prices; and that the offeror must think the target is a good investment or it would not be willing to pay a premium above market. While management communications are regulated by the Williams Act, the courts have not found these communications unlawful.[107] Moreover, the Supreme Court has held that an offeror has no implied right of action to sue target management for damages.[108]

The usefulness to shareholders of these target management communications is dubious at best. According to efficient capital market theory, a firm's operating performance and future prospects are already reflected in the price of its stock. Similarly, the claim that the target stock is undervalued and that the tender offer price is therefore inadequate lacks credibility. Finally, the frequent assertion that the willingness of an outsider to pay a premium demonstrates that the target is a good investment ignores the fact that an outsider's willingness to pay a premium often depends on securing new management.

2. Dividends and stock splits.—Management frequently responds to a tender offer by declaring either a stock split or a dividend in an attempt to increase the price of target shares. Stock splits do not alter the proportionate ownership of the corporation and therefore provide no economie benefit to shareholders. Nevertheless, stock splits are an accepted defensive tactic because of the belief that shareholders will be

105. Ebeid, *Tender Offers: Characteristics Affecting Their Success*, 11 MERGERS & ACQUISITIONS, Fall 1976, at 21, 25.

106. Schmults & Kelly, *Cash Take-Over Bids—Defense Tactics*, 23 BUS. LAW. 115, 122 (1967).

107. *E.g.*, Emhart Corp. v. USM Corp., 403 F. Supp. 660, 662 (D. Mass. 1975); Gulf & W. Indus., Inc. v. Great A. & P. Tea Co., 356 F. Supp. 1066, 1071 (S.D.N.Y.), *aff'd*, 476 F.2d 687 (2d Cir. 1973).

108. Piper v. Chris-Craft Indus., Inc., 430 U.S. 1 (1977).

confused by the split due to the "frailties of investor psychology."[109] In an efficient capital market, however, a stock split that does not enhance the value of the firm should not increase share prices. Empirical evidence supports this conclusion. In a famous study of stock splits, Fama, Fisher, Jensen, and Roll[110] found that increases in share value after stock splits were attributable to investor confidence about future earnings rather than to multiplication of shares. Thus, it is highly doubtful that a stock split in response to a tender offer with no prospect of increased earnings will affect share prices.

The efficacy of a dividend increase is also far from clear. At the very least, the firm must have adequate surplus to declare a dividend. A dividend of less than the premium offered by the offeror may have little impact, particularly with institutional investors who are likely to be more interested in capital appreciation than dividends.[111] More fundamentally, dividend increases or decreases by themselves should have no effect on the value of a firm's securities. As Miller and Modigliani have demonstrated,[112] a firm's earnings, rather than its dividend policy, determine the market valuation of its securities. Both dividend increases and stock splits are unlikely to raise the value of a target's securities, therefore, absent an increase in earnings. Nevertheless, both tactics may have some strategic value in defeating a tender offer. Dividends may deplete the corporation of excess cash that made it attractive to the offeror in the first place; stock splits may give the target an opportunity to remove stock certificates from circulation temporarily and thereby prevent shareholders from tendering during the duration of the offer.

3. Corporate purchase of shares.—When a corporation purchases its own shares (either by open market purchase or tender offer), shares that otherwise might be tendered go out of circulation. While this technique is not without risk since a reduction of the outstanding stock also reduces the amount needed by an outsider to gain control, this risk is eliminated if the stock can be placed in friendly hands.

Corporate purchase of shares is subject to some federal regulation. Since management is clearly an insider, failure to disclose material in-

109. E. ARANOW & H. EINHORN, TENDER OFFERS FOR CORPORATE CONTROL 246 (1973).

110. Fama, Fisher, Jensen & Roll, *The Adjustment of Stock Prices to New Information*, 10 INT'L ECON. REV. 1 (February 1969).

111. E. ARANOW & H. EINHORN, *supra* note 109, at 245.

112. Miller & Modigliani, *Dividend Policy, Growth, and the Valuation of Shares*, 34 J. BUS. 411 (1961).

formation should be actionable under rule 10b-5.[113] Corporate purchases of stock may also be a manipulative practice violative of section 9(a)(2) of the 1934 Act if undertaken only to frustrate a tender offer.[114] Finally, rule 13e-1 prohibits an issuer from repurchasing shares during the course of a tender offer made by any other person unless the issuer has filed an information statement with the SEC.[115]

The propriety of corporate repurchases to maintain control has also been challenged under state law. A series of Delaware cases,[116] typified by the famous case of *Cheff v. Mathes*,[117] have held that directors can lawfully expend corporate funds to purchase shares at premium prices during a contest for control provided a "corporate policy" is at stake. If directors believe in good faith that the outsiders will change corporate policy to the detriment of the corporation, and do not merely want to perpetuate themselves in control, stock purchases are justified.[118]

As numerous commentators[119] have pointed out, the distinction between purchases for policy and personal reasons is virtually impossible to draw since there will rarely be a case where "the incumbent management has admitted that it was fighting merely to preserve its position for its own benefit."[120] The result is that directors can attempt to thwart a control bid by purchasing shares with relative impunity if they document their actions with self-serving declarations about corporate policy.

4. *Corporate issuance of shares.*—When a corporation increases the amount of outstanding stock, it increases the minimum number of

113. *E.g.*, Ruckle v. Roto American Corp., 339 F.2d 24 (2d Cir. 1964). If no deception is alleged, however, corporate purchases of stock to perpetuate control are not actionable under rule 10b-5. Santa Fe Indus., Inc. v. Green, 430 U.S. 462 (1977).

114. *E.g.*, Crane Co. v. Westinghouse Air Brake Co., 419 F.2d 787 (2d Cir. 1969), *cert. denied*, 400 U.S. 822 (1970).

115. The issuer is also required to transit the specified information to its shareholders. Rule 10b-13, 17 C.F.R. § 240.10b-13, (1978), prohibits a person making a teuder offer for an equity security from purchasing such security other than pursuant to the tender offer itself. *See* E. ARANOW & H. EINHORN, *supra* note 109, at 236-37.

116. *E.g.*, Cheff v. Mathes, 41 Del. Ch. 494, 199 A.2d 548 (1964); Kors v. Carey, 39 Del. Ch. 47, 158 A.2d 136 (1960); Martin v. American Potash & Chem. Corp., 33 Del. Ch. 232, 92 A.2d 295 (1952).

117. 41 Del. Ch. 494, 199 A.2d 548 (1964).

118. The test is virtually identical to the one used to determine when corporate funds can be used to pay management's expenses in a proxy fight. *See, e.g.*, Rosenfeld v. Fairchild Engine & Airplane Corp., 309 N.Y. 168, 128 N.E.2d 291 (1955).

119. *E.g.*, Israels, *Corporate Purchase of Its Own Shares—Are There New Overtones*, 50 CORNELL L.Q. 620 (1965); Note, *Buying Out Insurgent Shareholders With Corporate Funds*, 70 YALE L.J. 308 (1960).

120. Marsh, *Are Directors Trustees?*, 22 BUS. LAW. 35, 60 (1966).

shares necessary to obtain control. Any stock interest acquired by an outsider in anticipation of a tender offer is also diluted. If the new stock is issued to parties friendly to incumbent management, the prospect of a successful tender offer is significantly decreased.

Unlike corporate repurchases, the Williams Act does not directly regulate the issuance of shares. However, failure to disclose that additional shares have been issued during the course of a tender offer may violate section 14(e).[121] The issuance of shares may also breach fiduciary duty under state law if the purpose of the issuance is to obtain or maintain control.[122] As in the case of corporate purchases, therefore, the legality of issuances of shares to thwart control by an outsider turns on whether management acted to preserve corporate policy or to perpetuate itself in office, an unworkable test.

5. Institution of legal proceedings.— Targets threatened by a tender offer often resort to the courts. Whether the underlying claim is meritorious or not, a lawsuit can be a powerful defensive tactic. As one commentator has stated:

> A lawsuit becomes a focal point for rallying the troops. Everyone can feel good—"we're doing something. We're hitting back. Boy, we really have got something there to protect us." And people will then start to function again in a real way to see what actually can be done to defend against this tender, which defense may not be in the courthouse at all.[123]

Although the possible subjects of a lawsuit brought by a target are virtually endless,[124] the two most important are suits for alleged Williams Act violations and suits for alleged antitrust violations.

Until recently, it appeared that a target company could sue an offeror for Williams Act violations and either recover damages[125] or obtain injunctive relief.[126] The ability of targets to sue offerors for disclosure omissions or misstatements, particularly over such vague questions as whether the offeror disclosed its future plans, considerably chilled tender offers. The Supreme Court's decision in *Chris-Craft*, however, arguably changes this situation.

In *Chris-Craft*, the Court held that an offeror could not sue a tar-

121. *See, e.g.*, Klaus v. Hi-Shear Corp., 528 F.2d 225 (9th Cir. 1975).

122. *E.g.*, Condec Corp. v. the Lunkenheimer Co., 43 Del. Ch. 353, 230 A.2d 769 (1967).

123. Wachtell, *Special Tender Offer Litigation Tactics*, 32 BUS. LAW. 1433, 1438 (1977).

124. For a list of the wide variety of lawsuits in the tender offer context, see E. ARANOW, H. EINHORN, & G. BERLSTEIN, *supra* note 3, at 199.

125. *E.g.*, H.K. Porter Co. v. Nicholson File Co., 482 F.2d 421 (1st Cir. 1973).

126. *E.g.*, Electronic Specialty Co. v. International Controls Corp., 409 F.2d 937, 944-46 (2d Cir. 1969).

get for damages to remedy Williams Act violations. A common refrain in the legislative history of the Williams Act is the congressional intention "to avoid tipping the balance of regulation either in favor of management or in favor of the person making the takeover bid."[127] If the Court were to hold that a target could sue an offeror for Williams Act violations, but under *Chris-Craft* an offeror had no corresponding remedy, the balance would be tipped decidedly in the target's favor. If a target has no implied right of action to sue an offeror for damages after *Chris-Craft*, the efficacy of litigation to redress alleged Williams Act violations will be considerably diminished.

Case law has diminished the target's ability to sue for injunctive relief for alleged Williams Act violations in another respect. In *Rondeau v. Mosinee Paper Corp.*,[128] the Court held that a showing of irreparable harm was necessary to obtain permanent injunctive relief against an offeror who had failed to file a timely section 13(d) statement. The Court emphasized that the purpose of the Williams Act is to provide shareholders with adequate information and not to provide management with a weapon to discourage takeover bids. After *Rondeau*, therefore, it will be significantly more difficult for targets to obtain permanent injunctive relief against offerors. Even if a court finds that an offeror has made inadequate or misleading disclosures, *Rondeau* suggests that the offeror should be allowed to correct these omissions or misstatements rather than be subject to permanent injunction from making a tender offer. While *Rondeau* concerned standards for obtaining a permanent injunction rather than the more typical request for a preliminary injunction, courts have generally allowed offerors to continue their tender offer activities after making required corrections when preliminary injunctive relief is requested.[129]

Along with alleged Williams Act violations, targets frequently seek to enjoin tender offers on antitrust grounds. Because the antitrust laws as currently interpreted condemn a merger of competitors with relatively small market shares under section 7 of the Clayton Act,[130] many tender offers have been open to antitrust attack.

The ability of a target to delay or defeat a tender offer on the theory that it would violate section 7 of the Clayton Act, however, has also been called into question by recent developments. To obtain injunctive relief under section 16 of the Clayton Act, a party must establish "loss

127. S. REP. No. 550, 90th Cong., 1st Sess. 3 (1967).
128. 422 U.S. 49 (1975).
129. *See* E. ARANOW, H. EINHORN, & G. BERLSTEIN, *supra* note 3, at 133.
130. Brown Shoe Co. v. United States, 370 U.S. 294 (1962).

or damage by a violation of the antitrust laws." The question is whether target companies facing a tender offer can meet this standard. If targets must demonstrate that they have suffered antitrust injury (such as a loss of competitive position) to have standing to sue for injunctive relief,[131] their task will be difficult indeed.[132] If, on the other hand, a target need show only that the tender offer would injure the public, or that the target itself would be injured in some general way, standing to sue for injunctive relief would be far easier to establish.

The Supreme Court's recent decision in *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*[133] sheds some light on what showing is necessary to establish standing. In this treble damages action, the Court held that private antitrust plaintiffs had to show more than a worsening of their position as a result of a violation of section 7 of the Clayton Act in order to recover damages. An antitrust plaintiff must show some connection between the violation and the injury.[134]

If *Brunswick* is extended to suits for injunctive relief, target company injuries that result from tender offers, such as loss of independent identity, adverse impact on employee morale, and management preoccupation with the tender offer, are not antitrust injuries and would not be adequate to confer standing. A more difficult problem is presented by a claim by target management that target shareholders will suffer injury in a later divestiture or treble damage action. Under this theory, target management could argue that bringing an antitrust action is consistent with its fiduciary duty to protect its shareholders. While the argument has some surface appeal, it is not entirely persuasive. The presumed desire of management to perpetuate itself in office makes a claim by management that it is only fulfilling its fiduciary duties by

131. Courts have held that plaintiffs must allege anticompetitive injury in order to have standing to sue for damages. *E.g.*, Reibert v. Atlantic Richfield Co., 471 F.2d 727 (10th Cir.), *cert. denied*, 411 U.S. 938 (1973).

132. Missouri Portland Cement Co. v. Cargill, Inc., 498 F.2d 851, 866-67 (2d Cir.), *cert. denied*, 419 U.S. 883 (1974). As Judge Friendly stated in commenting on an antitrust defense raised by Missouri Portland Cement in response to Cargill's tender offer:

> Here again the uninitiated would find it somewhat difficult to discern what "loss or damage" Cargill's tender offer could inflict on MP [the target company] as a corporation, as distinguished from its management. A cornerstone of MP's antitrust argument is that acquisition of control by Cargill would make MP not too weak but too strong.

Id.

133. 429 U.S. 477 (1977).

134. The Court stated that an antitrust plantiff

> must prove more than injury casually linked to an illegal presence in the market. Plaintiffs must prove *antitrust* injury, which is to say injury of the type of the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful. The injury should reflect the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation.

Id. at 489.

bringing an antitrust suit highly suspect. Moreover, avoidance of a future divestiture or treble damages claim as a justification for an antitrust challenge is by its very nature highly speculative and therefore may not constitute antitrust injury. Any injury caused by divestiture or a treble damages judgment would be limited to nontendering shareholders—tendering shareholders have no further interest in the target. A solution that would avoid enjoining tender offers based on speculative future divestiture or damage actions, while at the same time protecting the rights of nontendering shareholders, is to allow shareholders an action against the offeror after the value of their investment has declined as a result of a successful claim under section 7 of the Clayton Act.[135] This solution has the added advantage of protecting shareholders who may be injured while at the same time preventing target management from frustrating the operation of the market for corporate control.

6. Defensive mergers.—One of the most frequent, and most effective, defensive tactics is the negotiation of a defensive merger. A defensive merger is a merger of the target company with a company other than the offeror, calculated to defeat the tender offer. Unlike most other defensive tactics, a defensive merger actually may benefit shareholders primarily because of its tax advantages.[136] If the compensation received by shareholders in a defensive merger roughly approximates the terms of the tender offer, shareholders may be unwilling to tender their shares. Since most states require a shareholder vote to approve a merger, shareholders have a choice between voting for the merger or tendering their shares. In response to an attempt by management to effectuate a defensive merger, an offeror may raise the tender offer price or offer a merger proposal itself. These developments can only benefit shareholders. Thus, defensive mergers are unique among defensive tactics because they create an auction between the offeror and other companies interested in merging with the target to the ultimate advantage of all shareholders.

If management urges shareholders not to tender because of pending merger negotiations that do not in fact exist, it will be liable under section 14(e) and possibly also under common law fiduciary principles.

135. The likelihood of a successful § 7 suit has been somewhat diminished by the enactment of the Antitrust Improvements Act, 15 U.S.C. § 18a (1976). Under the Act, the offeror in a cash tender offer involving companies of sufficient size must file certain information with the FTC in order to allow the Justice Department and the FTC to evaluate in advance the offer's antitrust consequences..

136. E. ARANOW & H. EINHORN, *supra* note 109, at 258.

Similarly, management may be liable under federal law if it recommends one offer over another for the purpose of perpetuating itself in control.[137]

VI. State Law Remedies for Management Defensive Tactics: Toward a New Standard of Fiduciary Duty

Federal law does little to restrain the defensive tactics of incumbent management. Misrepresentations and omissions in management statements may be actionable under federal securities laws. The Supreme Court's decision in *Santa Fe Industries, Inc. v. Green*,[138] however, precludes liability for breach of fiduciary duty for persons who control a corporation under federal law if there is full disclosure. Thus, absent some deficiency in disclosure, fiduciary concepts under state law regulate defensive tactics.

A. Whether Defense of Control Is a Legitimate Justification for Corporate Conduct

Courts usually pay lip service to the notion that management action for the purpose of retaining control is a breach of fiduciary duty. The harder question is whether management should be allowed to use corporate funds to contest control whenever the dispute is over "policy."[139] Recognition of this policy justification for defense spending, an approach followed by the Delaware courts, is singularly unsatisfactory. First, the policy test is unworkable since virtually any management fight to retain control can be cloaked in self-serving declarations of corporate policy. Second, even if it is assumed that an outsider would pursue policies harmful to the corporation if in control, it is not clear that self-interested management should be allowed to thwart a control bid. Once an outsider gains control, new management has the same incentive to maximize the welfare of shareholders as any other management team. If the outsider is in fact a "raider," its conduct will be subject to sanction under standard fiduciary principles.[140] While an after-the-fact remedy may be more costly than a preventive remedy in deterring the true raider, it does possess the considerable advantage of

137. Grossman, Faber & Miller v. Cable Funding Corp., [1974-75 Transfer Binder] FED. SEC. L. REP. ¶ 94,913 (D. Del. 1974).
138. 429 U.S. 814 (1977).
139. *See* text accompanying notes 116-20 *supra*.
140. Brudney, *Fiduciary Ideology in Transactions Affecting Corporate Control*, 65 MICH. L. REV. 259, 274-75 (1966).

not allowing management an opportunity to frustrate legitimate takeover attempts in the guise of protecting corporate policy.

Apart from its unworkability and the availability of other remedies, the policy test is flawed by an even more fundamental defect. The policy test amounts to a concession that it is appropriate for incumbent management to decide for the shareholders who should manage the corporation. While the efficacy of shareholder voting in the modern publicly held corporation may be questioned, shareholder voting is crucial in the market for corporate control. Only if shares can be freely bought and sold will the market for corporate control function efficiently. If management is allowed to engage in defensive tactics that impede the ability of shareholders to trade their shares, the effectiveness of the market for corporate control will be severely hampered. Allowing management to frustrate the operation of the market for corporate control decreases management's incentive to maximize the return to shareholders.

An additional ground for prohibiting management action in defense of control is the difficulty of determining which shareholders management is representing. In most contested tender offer situations, one group of shareholders is willing to sell while another group is not, either because of loyalty to current management or the belief that a better offer will be forthcoming.[141] These two groups of shareholders have widely divergent interests. For the shareholders who wish to tender, any management interference is unwelcome, even if there is a valid corporate policy at stake. Since these shareholders will no longer have a continuing investment after they tender,[142] they are essentially indifferent to what new management will do. To represent the interests of these shareholders, therefore, management should take no action to frustrate the tender offer.

Allowing management to justify the use of defensive tactics financed with corporate funds during a contested tender offer to retain control by reference to a policy dispute is, therefore, unacceptable. At first glance, this conclusion may appear to be inconsistent with the principle that directors can spend corporate funds in a proxy contest to defend their control. The inconsistency, however, is more apparent than real. In a proxy contest, the use of corporate funds is justified at

141. *See* Weiss, *Tender Offers and Management Responsibility*, 23 N.Y.L. SCH. L. REV. 445, 452-55 (1978).

142. If a tender offer is oversubscribed, tendering shareholders may retain a continuing investment because the offeror will only accept shares pro rata. Shareholders can eliminate this risk, however, by selling to arbitrageurs or otherwise selling in the market.

least in theory[143] by the policy that the shareholders should be informed when casting their votes. Successful insurgents can also be reimbursed by the corporation for their proxy expenses.[144] Once informed, however, shareholders have the power to exercise their franchise and determine whether the incumbents or insurgents should manage the corporation. The precise opposite is true of many defensive tactics employed by incumbent management in a contested tender offer. Of all the defensive tactics, only shareholder communications can arguably be analogized to the proxy fight situation as necessary to inform shareholders. Most defensive tactics in the tender offer context effectively disenfranchise shareholders, or at the very least dilute shareholder voting power. If insiders, for example, amend the charter or bylaws to make the corporation unpalatable to outsiders, or purchase or issue shares, target shareholders are denied a meaningful opportunity to decide who should manage the corporation. This result is an affront to the principle of shareholder suffrage where it is most important—in the market for corporate control.

B. The Problem of Determining When Management Conduct Is Undertaken for the Purpose of Perpetuating Control

If perpetuation of control is an impermissible justification for management defensivc tactics, the problem becomes determining when a course of conduct is motivated by a desire to maintain control. It is necessary, in other words, to ascertain whether managemcnt conduct, ostensibly intended to benefit the corporation, was actually undertaken at least in part to preserve control. Management, for example, may issue shares pursuant to a stock option plan or asset acquisition and claim that any impact on control is incidental to the furtherance of a legitimate corporate purpose. Similarly, management may institute litigation on the grounds that it will benefit shareholders by preventing or remedying a violation of law.

When conduct by incumbent management during a contest for control is challenged, the initial quesiton is whether to appraise this conduct under the business judgment rule or a stricter standard because of management's self-interest. Because of competition in the capital and product markets, the market for corporate control, and manage-

143. The theory justifying expenditure of funds in a proxy contest has been seriously questioned. *See, e.g.*, Brudney, *supra* note 140, at 282. *Contra*, Rosenfeld v. Fairchild Engine & Airplane Corp., 309 N.Y. 168, 128 N.E.2d 291 (1955).

144. *Cf.* Rosenfeld v. Fairchild Engine & Airplane Corp., 309 N.Y. 168, 128 N.E.2d 291 (1955) (a shareholders' voted approved reimbursement).

ment's desire to maximize its compensation and stature, management generally has an incentive to act in the best interests of shareholders. When these pressures are effective, the business judgment rule, which serves as a quasi-jurisdictional barrier to the second-guessing of management behavior by the courts, serves a salutory function.[145] But the congruence of interests between management and shareholders breaks down in a contest for control. The obvious conflict of interest between the interests of management, primarily interested in perpetuating themselves in office, and the interests of shareholders, primarily interested in either selling their shares at the highest price possible or participating in a firm with more efficient management,[146] suggests that the business judgment rule is inapposite in a contested control situation.

If the business judgment rule is an inappropriate standard for management conduct during a tender offer, a prophylactic rule that prohibited any corporate action that affected control would unnecessarily deprive the corporation of advantageous opportunities. A compromise position is required. Management should be able to take action that has the effect of preserving its control only if there is an overriding or compelling corporate purpose to justify the conduct at the time. The burden of proving an overriding or compelling business purpose should rest on management in light of their self-interest in retaining control.[147]

The recent case of *Klaus v. Hi-Shear Corp.*[148] presents a good example of the operation of the compelling necessity standard. During a takeover attempt, target management approved, along with other defensive tactics, the formation of an Employee Stock Ownership Trust (ESOT). Management then donated 30,000 treasury shares to ESOT and guaranteed a bank loan with which ESOT purchased another 50,000 shares at market value. As a result of this stock issuance, the tender offeror controlled a smaller percentage of the total stock. The Ninth Circuit rejected application of the business judgment rule and held that there was no "compelling business purpose" to justify the for-

145. Manne, *Our Two Corporate Systems: Law and Economics*, 53 U. VA. L. REV. 259, 270-71 (1967).

146. It is conceivable, of course, that some shareholders may have a sentimental or other noneconomic attachment to incumbent management. Presumably, however, this situation will occur more frequently in closely held corporations.

147. By contrast, the actions of the offeror in deciding to tender and setting the tender price should be evaluated under the more lenient business judgment rule. The conflict of interest between management and shareholders and between the various classes of shareholders that justify a higher standard for target management are absent in the case of the offeror. Thus the actions of the offeror should not come under any greater scrutiny than the normal corporate decision typically entrusted to management's discretion.

148. 528 F.2d 225 (9th Cir. 1975).

mation of ESOT.[149]

Northwest Industries, Inc. v. B.F. Goodrich Co.[150] illustrates the opposite judicial approach. In response to an exchange tender offer by Northwest Industries, Goodrich hastily entered into an agreement with Gulf Oil, its partner in a joint venture, to purchase Gulf's interest in the joint venture for 700,000 shares of Goodrich common stock. Northwest attempted to block the delivery of stock to Gulf on the theory that the consideration paid for Gulf's interest, the 700,000 shares, was grossly inflated to ensure that a substantial block of stock would be held by interests friendly to Goodrich. The Court rejected this claim, holding that the action by Goodrich's management was protected by the business judgment rule.[151] By failing to recognize the conflict of interest of Goodrich's management, the Court effectively placed the burden of proving fraud on the offeror. Under this standard, management conduct that has the effect of preserving control will almost inevitably be insulated from meaningful judicial scrutiny.

The compelling business purpose test with the burden of proof on management is more consistent with the inevitable conflict of interest faced by management in a contested control situation. Adoption of this test would subject many defensive tactics to claims of breach of fiduciary duty, a radical departure from much of existing law. Several courts, for example, have stated that target management has not only the right, but also the duty to oppose control bids that it does not believe to be in the best interests of the corporation.[152] By this standard, the failure to resist a tender offer may constitute a breach of fiduciary

149. Hi-Shear did not suggest any compelling reason why ESOT

> had to be established at a time so advantageous to those in control rather than a few months later when it would not have caused a severe injury to [the offeror] . . . . [T]he purported business purpose of the issuance of shares to ESOT was not sufficiently compelling to outweigh the unfair advantage to management at [the offeror's] expense.

Id. at 234. The court found that several other stock issuances served a compelling business purpose.

150. 301 F. Supp. 706 (N.D. Ill. 1969).

151. Northwest's tender offer announcement galvanized Goodrich and Gulf to complete the purchase at this time. Although the officers of both Goodrich and Gulf claim there was no mutual agreement to defeat plaintiff's takeover bid, there was remarkable empathy between the companies. On the other hand, Northwest appears unable to establish that Goodrich officials' desire to remain in office was the sole or the primary motivation for their decisions.

> Plaintiff has not shown any likelihood that it can prove that the transaction amounts to fraud. Considering all factors of value, the persuasive evidence indicates that . . . [Goodrich paid] a fair price for Gulf's one half of Chemicals. Goodrich's officers and directors appear to have been exercising their honest business judgment, so that their decision is conclusive.

Id. at 712.

152. *See, e.g., id.*

duty unless management can justify its inaction. The compelling business purpose test would reverse the presumption and require management to justify the use of defensive tactics.[153]

VII. Conclusion

The cash tender offer is at present the principal mechanism in our economy for the transfer of control to those who expect to manage the assets of a corporation more profitably. The existence of this mechanism gives incumbent management an incentive to perform well and keep stock prices high, but the incentive is lessened to the extent that federal and state law hinders potential managers from using the cash tender offer to gain control. The Williams Act limits the effectiveness of the cash tender offer by imposing a quasi-fiduciary duty on the offeror despite the absence of an insider relationship with the target company. State takeover statutes contain provisions similar to those of the Williams Act, but go further to eliminate the element of surprise generally necessary for a successful tender offer and, in some cases, to let target company management exercise a great degree of control over the struggle with the tender offeror. These statutory and regulatory impediments to the smooth functioning of the market for corporate control serve no valid purpose.

Incumbent managements have also been free, under state corporation statutes and caselaw governing management accountability to shareholders, to employ an array of defensive tactics to frustrate tender offers. Despite the obvious conflict of interest of incumbent management faced by an unwelcome tender offer, and the conflict of interest between different classes of shareholders, courts have typically applied the business judgment rule in evaluating management conduct. In some recent cases, however, courts have recognized the inappropriateness of that rule in the cash tender offer context and have required that

153. The extent to which types of defensive tactics would survive the compelling business purpose standard varies with the particular defensive tactic involved. Courts may draw a distinction between defensive tactics that have been approved by shareholders and those that have not. A court, for example, might be justifably reluctant to interfere with a charter amendment approved by shareholders if management has made full disclosure concerning the amendment's implications. *See* notes 102-04 *supra* & accompanying text.

An additional problem faced by courts will be formulating an appropriate remedy for improper management defensive tactics. Shareholders of the target corporation may sue for either loss of the tender offer premium, waste of corporate funds, or injunctive relief. Offerors may also be able to sue under state law for the value of the loss of a control block in the target or for injunctive relief.

management conduct likely to undermine the tender offer satisfy a compelling business purpose test. Application of this standard appears to be the most promising means under present law, absent legislative reform, to preserve the required vitality of cash tender offers.