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Defensive Take-over Procedures
Since the Williams Act*

W. MC NEIL KENNEDY**

The enactment of the Williams Act1 (the Act) has had a significant impact on defensive take-over bid techniques. Although many of the Act's supporters believed that the Act would materially assist target companies in combating tender offers, initial experience under the Act has shown that the opposite is true. Prior to the Act, bidders had few, if any, guidelines to follow and hence, almost every aspect of their conduct could be questioned and contested. The Act changed this, and now, generally speaking, bidders have specific disclosure and substantive requirements that can be followed with relative ease. In the past, there was little effective regulation as to what target companies said or did defensively. Now, however, regulation of target company tactics has placed them under two fairly severe handicaps. As will be shown, target companies are placed at a time disadvantage, because they must file certain statements with the Securities and Exchange Commission (SEC) before they can effectively communicate with their shareholders, and furthermore, the present regulations do not provide sufficient guidance in terms of what target companies can and must disclose to their shareholders.

This article is concerned with the Act as passed by Congress in the form of amendments to the Securities Exchange Act of 1934 and with the temporary regulations enacted by the SEC immediately after the bill became law.2 Although still classified as "temporary," these regulations have been revised

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** Of the firm of Pope, Ballard, Kennedy, Shepard & Fowle, Chicago; J.D., Ohio Northern University, 1930; Chairman, ABA Committee on Federal Regulation of Securities; Member, Ohio and Illinois bars.
Defensive Take-over Procedures

(housekeeping changes with little substantive impact) by the SEC a number of times and are not likely to be replaced by permanent regulations in the near future. One reason for this is the SEC's apparent dissatisfaction with certain provisions of the Act.

In passing the Act Congress evidently believed that the SEC already possessed sufficient authority to regulate bids made through the offer of securities and hence such bids were specifically exempted from the disclosure requirements. By so doing Congress also exempted the defensive maneuvers of target companies from these sections and particularly from the provisions of Section 14(d)(4) which regulate recommendations to accept or reject take-over bids. Because of this dual congressional treatment, this article will approach target company techniques in two distinct arenas: defense of cash tender offers and defense of tenders in general (security and cash tenders).

Target Company Recommendations on Cash Tender Offers

The Act as it applies to target companies involved in cash offers does not force target companies to recommend for or against the offer. Silence or neutrality is, therefore, permissible under the provisions of the Act. This statement must be qualified, however, for at least two reasons. First, under either state corporate law or an expanded interpretation of Rule 10b-5 or Section 14(e), it could be argued that if management of the target company is aware of any material, nonpublic information about the company, either favorable or unfavorable, it has a duty to come forward and disclose this. It is hard to visualize a court holding that the management has any duty to the outsider making the tender offer whereas a court could easily impose this duty upon management with respect to its own shareholders. Hence, it would seem to be advisable for the directors of a target company to reveal previously nonpublic information which would materially affect the judgment of its shareholders in determining whether to accept or reject the tender offer, unless there is some strong corporate reason to withhold disclosure.

Second, the SEC does not appear to be satisfied with the ability of management to remain silent and is endeavoring to develop rules designed to force, or at least induce, management of a target company to make a recommendation for or against the bid. An example of this is found in Rule 14d-2 (f). This rule permits a target company to send to its security holders a letter which does no more than identify the tender offer and state that management is studying the matter and will, on or before a specific date which

must be no later than ten days prior to the date the tender offer expires, advise the shareholders as to management's recommendation to accept or reject the offer. The letter may also request security holders to defer making a determination until they receive management's recommendation. If management does send out such a letter, it obligates itself to make a recommendation to accept or reject; it precludes itself from making no recommendation at all. To induce management to decide that it will make a recommendation for or against before it even studies the matter seems unwarranted. A careful study may reveal that such a recommendation is not in order or after such a study management may split on whether it should make such a recommendation.

Once management decides to make a recommendation to its securities holders to accept or reject the tender offer, Rule 14d-4\textsuperscript{7} prevents management from acting until it has filed a Schedule 14D\textsuperscript{8} with the SEC. This is a shortened form of Schedule 13D\textsuperscript{9}—which is filed by the bidder—and is patterned after Schedule 14B\textsuperscript{10} under the proxy rules.\textsuperscript{11} Information required in Schedule 14D consists of identification of the securities sought by the bidder, the tender offer itself, the person filing the statement and the persons employed to make the solicitation or recommendation; the schedule also requires a statement of the reasons for the recommendation to accept or reject the tender offer and a description of any arrangements the person making the solicitation has with either the issuer of the securities involved or with the maker of the tender offer; if the schedule is filed by a corporation, it must list all its transactions, and those of its subsidiaries, its officers, its directors, and its affiliated persons in the securities of the issuer during the preceding sixty days. Moreover, copies of written solicitation material submitted to shareholders must be filed as an exhibit to this schedule. If the schedule is filed by a corporation, information need not be given concerning each officer, director, and controlling person of such corporation except as to certain purchases of securities required by Item 5. This differs from Schedule 13D which requires, in the introductory notes, that certain information be included in the schedule concerning officers, directors and controlling persons of the corporation filing it.

\textsuperscript{7} 17 C.F.R. § 240.14d-4 (1969).
\textsuperscript{10} 17 C.F.R. § 240.14a-102 (1969).
\textsuperscript{11} During the congressional hearings on the bill, a number of authorities criticized its attempt to compare tender offers to proxy contests. \textit{Hearings on S. 510 Before the Subcomm. on Securities of the Senate Banking and Currency Comm., 90th Cong., 1st Sess.} 116 (Robert Mundheim), 118 (Stanley Kaplan) (1967) [hereinafter cited as \textit{Hearings on S. 510}]. \textit{See also id.} at 84 (Philip West of NYSE), 98 (Ralph Saul of AMEX). They were overruled by the Congress, however, and particularly by the SEC when it adopted the schedules to be used.
If there is any material change in the information contained in the schedule the person filing the schedule must promptly file an amendment under Rule 14d-4(b).\textsuperscript{12} Further, Rule 14d-4(c)\textsuperscript{13} requires that any written recommendation to accept or reject a tender offer must include a fair summary of some of the information contained in the Schedule 14D, such as the name of the person making the solicitation, identification of the tender offer, and a description of any soliciting arrangement the person has with the issuer or the maker of the tender offer.

Requiring that the Schedule 14D be filed prior to the time target company managements can effectively communicate with their shareholders places such managements (which prior to the Act could act immediately) at a distinct disadvantage. Although the information required in the Schedule 14D is not extensive, it does nonetheless take time to accumulate and prepare. Accordingly, I suggest all take-over candidates prepare these schedules now, have a system so that the information can be continually updated, and be ready to file them with the SEC at a moment’s notice.\textsuperscript{14}

The bulk of the items in the present Schedule 14D are straightforward, and will be relatively easy to answer. The only troublesome question is found in Item 1(b) requiring a statement of the reasons for the recommendation to accept or reject the bid. There being no present restrictions on management’s answer to this item, the door is left open to target companies to go all out in exposing the defects of the offer and to proclaim the virtues of their company. This item, of course, is the heart of most management campaigns against tender offers. It is also related to another consideration, namely, how much additional information might be required of management if it elects to recommend for or against the tender, particularly under the antifraud provisions of Section 14(e).\textsuperscript{15}

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Tender Offers in General: The Antifraud Provision
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A view of the Act and temporary rules as they apply to all take-over bids compels an examination of the antifraud section of the Act, Section 14(e).

\textsuperscript{12} 17 C.F.R. § 240.14d-4(b) (1969).
\textsuperscript{13} 17 C.F.R. § 240.14d-4(c) (1969).
\textsuperscript{14} Schedule 14D as presently drafted may be only the beginning. The SEC could eventually adopt an enlarged Schedule 14D which would include more of the information contained in Schedule 13D and in the proxy Schedule 14B. \textit{E.g.}, it may be desirable to require a listing of all purchases by the person filing the schedule of the securities of the target company during the preceding two years. \textit{Cf.} Item 3(c), Schedule 14B: “State with respect to the securities of the issuer purchased or sold within the past two years, the dates on which they were purchased or sold and the amount purchased or sold on each such date.” Also, perhaps something along the lines of Item 4(c) of Schedule 14B, requiring disclosure of any arrangement or understanding with respect to future employment or transactions, ought to be required.
This section is patterned after Section 10(b), but it differs from that section in that it is automatically operative and does not depend upon rules adopted under it by the SEC to become effective. Section 14(e) applies to both cash and stock take-over bids, and it applies to all bids irrespective of whether the stock sought is registered with the SEC under Section 12(g) of the 1934 Act. The coverage of this section, then, is considerably broader than the sections requiring the filing of Schedules 13D or 14D which apply only to securities registered under Section 12.

Prior to the adoption of Section 14(e), the federal courts generally believed that they did not have jurisdiction of actions brought under Rule 10b-5 involving take-over bids. Some, not many, target companies were able to hurdle this jurisdictional barrier, but except in a few instances the courts failed to grant relief.

As most observers predicted, the federal courts have now accepted jurisdiction under Section 14(e) of suits by offeree companies complaining that their opponent has engaged in some scheme in violation of the rule. The courts in time will also hear suits brought by offeror companies and, importantly, by injured shareholders of either company. Thus, as a result

18. Some target companies have had one of their shareholders who deposited his stock join as a plaintiff in the action. Use of this device has enabled at least one target company to obtain a temporary restraining order. See Moore v. Greatamerica Corp., 274 F. Supp. 490 (N.D. Ohio 1967). As this article went to press the United States District Court for the Southern District of New York granted a target company a preliminary injunction prohibiting a tender offeror from exchanging its securities for the stock of the target company. The court held that the target company had standing under Section 10(b) as well as Section 14(e) because the phrase "in connection with the purchase or sale of any security" of Section 10(b) "was intended by Congress to mean only that the device employed, whatever it might be, be of a sort that would cause reasonable investors to rely thereon, and, in connection therewith, so relying, cause them to purchase or sell a corporation's securities." Butler Aviation, Inc. v. Comprehensive Designers, Inc., CCH Fed. Sec. L. Rep. ¶ 92,543 at 98,487 (S.D.N.Y. 1969).
20. See Iroquois Indus., Inc. v. Syracuse China Corp., 417 F.2d 963 (2d Cir. 1969). But see Crane Co. v. Westinghouse Air Brake Co., CCH Fed. Sec. L. Rep. ¶ 92,532 (2d Cir. 1969) where the court stated that an unsuccessful tender offeror had standing under Section 10(b) because antitrust law would force the offerer to be an involuntary seller like the plaintiffs in Vine v. Beneficial Fin. Co., 374 F.2d 627 (2d Cir. 1967).
of Section 14(e), the former obstacles to federal jurisdiction have been removed. Target companies, therefore, will have easier access to the courts, but so will offeror companies and individual shareholders of both issuers.

Because the courts will be open to both sides, this article will first examine the exposure that target companies have as defendants and then discuss their role as plaintiffs. There have been only a few claims brought against offeree companies and their managements in the past. This is understandable since if offerors are unsuccessful in acquiring control they probably would be no more able to acquire the necessary shares through a lawsuit. Moreover, the effects of a tender offer on offerors is markedly different from the effect on offerees; the management of the offeror does not face extinction whereas the management of the offeree often does. Consequently, offerors are not prone to fight as doggedly as offerees and their managements. It would seem likely that, for these reasons, there will not be a material increase in litigation by offeror companies against offerees. It is highly probable, however, that shareholders of the offeree company, and perhaps the SEC, will be more aggressive in this area.

**Target Company Recommendations: Disclosure of Interests**

This brings us to the questions of whether target company management must make a recommendation to its shareholders, and, if it does, what it can say. At present, the Williams Act does not require a recommendation and no court has yet held that under either state or federal law management of the offeree is required to make such a recommendation to its shareholders in any type of take-over bid. Nor has any court yet held to the contrary but, as mentioned earlier, a court might impose such an obligation under circumstances when management is aware of very material undisclosed information. This is, however, a very complex area, and it is doubtful that there are any pat answers. For instance, what does target management do when it knows, or has reason to believe, that its earnings will be lower than the previous quarter? If it discloses this information it will probably make the offer more attractive, whereas management may honestly, and even correctly, believe that the offer is not in the best long term interests of their shareholders. Does target management, moreover, have any disclosure obligation under these circumstances to the offeror? As said before, it is doubt-

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21. E.g., Iroquois Indus., Inc. v. Syracuse China Corp., CCH Fed. Sec. L. Rep. ¶ 92,301 (W.D.N.Y. 1968); Kropp Forge Co. v. Anadile, Inc., Civil No. 67 C 715 (N.D. Ill. 1967). Most recently a suit for damages or injunctive relief or both was sustained by the Second Circuit under Section 10(b) and Rule 10b-5, Crane Co. v. Westinghouse Air Brake Co., CCH Fed. Sec. L. Rep. ¶ 92,532 (2d Cir. 1969).
ful. Although the SEC and the stock exchanges have been pushing for early disclosure of material information, there is no affirmative duty of disclosure under the federal law in the absence of trading by an insider.\textsuperscript{22} Perhaps the very least that should be required is for management to disclose what the officers and the directors intend to do themselves with respect to the tender offer.

The principal difficulty facing management of the offeree is how to satisfy its fiduciary obligation to its shareholders to make a full disclosure of its self-interest and motives when it makes any recommendation. This is especially true under the clause of Section 14(e) that requires complete disclosure in order to make other statements not misleading.\textsuperscript{23} Management is under this obligation to disclose fully its interests in its own company and any arrangements it has with the maker of the tender offer whether it is for or against the tender offer.\textsuperscript{24} As a result of Section 14(e), offeree managements will be more exposed to suits by their own shareholders on this score, and it is surprising that there have not been more suits in the past.

Of special interest in this connection are the decisions of the federal courts in the \textit{Mills v. Electric Auto-Lite Co.} case\textsuperscript{25} concerning proxy solicitations under Section 14(a). In that case, the district court held on a motion for summary judgment that a merger between Electric Auto-Lite and Mergenthaler Linotype Company was invalid because the Auto-Lite directors stated in the proxy statement that they had carefully considered and approved the terms of the merger and recommended to the shareholders its approval. The directors, however, according to the court, failed to disclose that the

\begin{footnotes}
\item[22.] See \textit{SEC v. Texas Gulf Sulphur Co.}, 401 F.2d 833, 848 (2d Cir. 1968). The SEC does have the authority to require disclosure under Section 13 of the 1934 Act, 15 U.S.C. § 78m (1964). Form 8-K is the vehicle used for disclosure under this section, but it does not have to be filed until the tenth of the month following the month in which the event occurred. The affirmative disclosure requirements are discussed in \textit{J. FLOM, B. GARFINKEL & J. FREUND, DISCLOSURE REQUIREMENTS OF PUBLIC COMPANIES AND INSIDERS} 13-49 (1967); \textit{Ruder, Guidelines to Solution of the Corporate Disclosure Dilemma, EMERGING FEDERAL SECURITIES LAW} 83, 87-90 (Nordin ed. 1969).
\item[23.] \textit{"It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading ..."} 15 U.S.C. § 78n(e) (Supp. IV, 1969).
\end{footnotes}
Directors of both Auto-Lite and Mergenthaler were under the control of a third party. The defendants appealed to the Seventh Circuit where the plaintiffs argued that the case should be upheld because the directors of Auto-Lite failed to disclose their divided loyalty. They relied primarily on the Supreme Court's decision in *SEC v. Capital Gains Research Bureau, Inc.*, and contended that when a fiduciary gives investment advice he must disclose all facts which create a conflict of interest with a potential for abuse. On this point, the Seventh Circuit upheld the decision and in some respects went even further than the district court.

The court said that the crucial question was not whether the advice given by the Auto-Lite directors was good, but whether the minority shareholders were sufficiently alerted to the board's relationship to their adversary. In ruling that as a matter of law there was not sufficient disclosure of the interlocking relationship, the court also felt that the language used and the position of the language in the proxy statement was not adequate to make full disclosure. Consequently, not only must disclosure of self-interest be made, but the disclosure should be as prominent as the recommendation. The Seventh Circuit went on to hold, however, that plaintiffs had not established a causal relationship between the violation and the vote on the merger. On January 20, 1970, the Supreme Court vacated the Seventh Circuit's opinion on the causation issue and remanded the case to the district court. Because the Court had not been asked to review whether the proxy statement was in fact materially misleading, it did not reach that question.

It is obvious, therefore, that management must be careful to disclose all its possible conflicts of interest in connection with a take-over bid. As a result of this requirement, the SEC should require in Schedule 14D more detailed disclosure so that offeree managements will have more explicit guidance on what they should reveal to their shareholders. This schedule could act as a standard for them against which their conduct would be judged.

**Target Company Recommendations: What Information Can Be Given?**

Assuming that offeree management does make sufficient disclosure of its self-interest, how far can it go in making its recommendation? It is here that offeree management exposes itself to suits by offerors and the SEC. Although I do not think we will see a significant increase in these suits, 26

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28. Id. at 434-35.
29. To obtain some idea of what other countries have considered necessary in these circumstances see Companies Act of 1961, § 184, sched. 10, Pt. C (Austl.); Securities Act of 1966, c. 142, § 95 (Can.).
30. See cases cited, note 21, supra.
there may be more of them as a result of Section 14(e). At least an offeror company’s complaint should now be able to withstand a motion to dismiss.\textsuperscript{31} Item 1(b) of Schedule 14D requires a statement of the reasons for the recommendation to accept or reject the tender. In addition, former SEC chairman Cohen stated, prior to the adoption of the bill, that in all fairness to the shareholders management should have a real opportunity to make its case with respect to the tender offer.\textsuperscript{32} Despite Item 1(b) and Mr. Cohen’s statement, the SEC’s approach will probably resemble the treatment accorded a 1933 Act registration statement, namely, projections and generally optimistic statements will be outlawed. This is also the position taken by the SEC with respect to the proxy rules. If the SEC does adopt that position, it will only highlight the inconsistent approaches taken by it when it operates under the 1933 Act registration provisions and when it enforces the disclosure requirements of the 1934 Act. If a mineral find is material under the 1934 Act, it is difficult to understand how it is immaterial under the 1933 Act, especially when the issuance of a statutory prospectus might, according to some persons, support liability under Rule 10b-5 of the 1934 Act. The Tenth Circuit’s decision in \textit{Sunray DX Oil Co. v. Helmerich & Payne, Inc.},\textsuperscript{33} is a striking illustration of the conflicting disclosure philosophies of the 1933 and 1934 Acts and the recent opinion of the District Court for the Eastern District of New York in \textit{Gerstle v. Gamble-Skogmo, Inc.}\textsuperscript{34} raises these same problems.

On balance, I think that the SEC should be more liberal in permitting offeree managements to state their reasons in opposition to tender offers. As will appear below, the courts have already exhibited a liberal approach in this area. For instance, there seems to be no reason why valuation studies should not be used, particularly if they form the foundation for management’s recommendation. In such a situation, it is difficult to conceive of more material information. In at least one advertisement opposing a tender offer, management has relied upon the opinion of an investment banker in recommending to shareholders that they reject the offer.\textsuperscript{35} The spectre of shareholder suits, moreover, will be a limiting influence restraining overzealous statements by target management.

\textsuperscript{31}\textit{See, e.g., Iroquois Indus., Inc. v. Syracuse China Corp., CCH Fed. Sec. L. Rep. ¶ 92,301 (W.D.N.Y. 1968), aff’d, 417 F.2d 963 (2d Cir. 1969).}
\textsuperscript{32} \textit{Hearings on S. 510 at 176.}
\textsuperscript{33} 398 F.2d 447 (1968).
\textsuperscript{34} 298 F. Supp. 66 (1969).
Recommendations to accept or reject take-over bids by target management are, of course, just the beginning. Target management generally has an uphill fight. For the most part the eventual outcome will be based on the market's reaction to the offer. This is particularly true where the shareholders of the target company consist of traders rather than investors. In such cases, the shareholders will most likely be anxious to dispose of their stock for an immediate profit instead of waiting for some long term potential gain offered by management. Consequently, one of the most important elements of a successful defense by target management is to be constantly aware of the possibility that a take-over bid may be made and continually foster the goodwill of its shareholders.

Once an offer is made, target management must then convince its shareholders that the offer is inadequate. When cash is offered, it will not do for target management to say simply that "Since X has offered $40 a share it must be worth more." This type of statement, without any real factual support, rarely convinces anyone to hold his stock.36 When securities are offered instead of cash, target management has more of an opportunity to show that the package is not very attractive. Moreover, in exchange offers, the target company has time to make the necessary investigation, while the offeror's registration statement is pending with the SEC. The target company's investment bankers and accountants will be of immeasurable assistance in helping it to evaluate the exchange offer. Target management will, in addition, want to make a thorough investigation of the offeror company. Then, based upon its investigation and analysis of the pending registration statement, the target company should communicate directly with the SEC, noting any defects in the registration statement or failures to make sufficient disclosure. There is some thought that target companies should not communicate with the SEC concerning the pending registration statement; instead, they should wait until the registration statement becomes effective and then file a lawsuit claiming that the registration is inaccurate and misleading. By operating in this manner, it is asserted that no affirmative defense can be raised by the offeror that the offeree's objections were considered and rejected by the SEC. This does not seem to be an advantageous procedure to follow. First, once the registration statement becomes effective, the courts will probably defer in large part to the judg-

36. In one instance target company management cooperated with the tender offeror's competitor in secret market manipulations to raise the target company's stock price high enough to make the tender offer unattractive. See Crane Co. v. Westinghouse Air Brake Co., CCH Fed. Sec. L. Rep. ¶ 92,532 (2d Cir. 1969).
ment of the SEC irrespective of whether target management submitted its comments to the SEC. Second, and importantly, careful and honest comments to the SEC will generally produce significant changes in the disclosures in the registration statement and perhaps even in the package of securities to be offered. This added disclosure might defeat the exchange offer. In any event, once the offer is made, whether it is cash or securities, a lawsuit becomes a distinct possibility.

Under the Williams Act, defensive management will also have direct access to the federal courts under Section 14(e). Although the courts will be open, target companies will not, in all probability, be considerably more successful in enjoining take-over bids now than they were prior to the Act. The Act merely opens the courts; it does not appear to give any additional basis for attacking the take-over bids. True, if the offeror makes a mistake and fails to disclose some material item, the attack should be successful. But now that offerors have been given a list of specific items that they must disclose, it seems unlikely that there will be many mistakes or omissions in their soliciting materials or schedules. The courts being open, however, imaginative counsel will have an opportunity to devise new claims that the courts will treat more sympathetically than the old ones.

In cash take-over bids, avenues of attack are open to defensive management on (1) the disclosure as to the offeror's future intentions with respect to the target company, (2) the disclosure of the offeror's financing, and (3) whether because of the expansive definition of "person" contained in Sections 13(d)(3) and 14(d)(2), all the Schedule 13D's have been filed by the "persons" participating in the offer. The Court of Appeals for the Second Circuit, however, was unsympathetic to similar claims in *Electronic Specialty Co. v. International Controls Corp.* Despite the findings of two different district court judges that International Controls had violated Section 14(e), the Second Circuit reversed stating that take-over situations resemble proxy contests and that under these circumstances it is unwise and unrealistic to impose strict standards on either party. The court applied the test it announced earlier in *Symington Wayne Corp. v. Dresser Industries*, namely, whether "any of the stockholders who tendered their shares would probably not have tendered their shares if the...[alleged violation] had not occurred."

41. 383 F.2d 840 (1967).
42. Id. at 843.
Recent events in the controversy over the Susquehanna Corporation's attempt to gain control of the Pan American Sulphur Company (PASCO), however, indicate a greater willingness on the part of both the courts and the SEC to define and regulate tender offer proceedings at an early stage. As a result of a successful tender offer announced on November 27, 1968, Susquehanna obtained 1,800,000 shares of the common stock of PASCO. PASCO brought suit in the United States District Court for the Western District of Texas alleging that various required filings made by Susquehanna with the SEC in connection with the tender offer contained representations that were false and misleading. The relief sought would require Susquehanna (1) to divest itself of the PASCO shares it has acquired or, in the alternative, be enjoined from voting these shares, and (2) to remove from the PASCO board the three Susquehanna designees (named as individual defendants) who were placed on the board by Susquehanna following the consummation of the tender offer.

As amended by the Williams Act, Section 13(d)(1) provides that any person who, after acquiring the beneficial ownership of any equity security of a class registered pursuant to Section 12 of the Exchange Act, is the beneficial owner of more than ten percent of such class must file with the SEC within ten days after such acquisition a statement containing certain particularized information. Section 13(d)(1)(C) specifies that if the purpose of the purchases of the securities is to acquire control of the business of the offeree, such filing, called a Schedule 13D, must include a statement of "any plans or proposals which such persons may have to liquidate such issuer, to sell its assets to or merge it with any other persons, or to make any other major change in its business or corporate structure . . . ." Susquehanna's Schedule 13D filings first disclaimed all intentions of pursuing any of these named possibilities, but then added that "if, at some subsequent time, it should appear the interests of the Pan American stockholders would be better served by any of the foregoing courses of action, Susquehanna may propose or adopt such course."

Susquehanna's actual intention, according to PASCO, was to use unencumbered assets of PASCO to make acquisitions of other companies, and/or cause a merger of PASCO with certain other companies. As evidence of this scheme, PASCO pointed to a December 10, 1968 telegram from Herbert F. Korholz, president of Susquehanna, to the directors of American Smelt-

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45. Plaintiff's Complaint at 14-15, id.
46. Id. at 4.
47. Id. at 12.
ing & Refining Company, representing that he had authority to speak for PASCO and proposing that PASCO was prepared to acquire all of the outstanding stock of American Smelting for more than $1.5 billion in PASCO securities.\textsuperscript{48} 

PASCO's motion for a preliminary injunction pendente lite was granted.\textsuperscript{49} Finding that PASCO had demonstrated a reasonable possibility that it will ultimately succeed at trial in establishing a violation of the Exchange Act, and a reasonable possibility that the Schedule 13D statements were false and misleading in a material way, the court enjoined Susquehanna from voting its PASCO shares and ordered that the composition of the PASCO Board of Directors remain unchanged.\textsuperscript{50} Rejecting Susquehanna's contention that the irreparable injury which a preliminary injunction would cause makes this remedy inappropriate, Judge Roberts concluded:

\begin{quote}
It is clear that a target corporation and its stockholders have standing to bring a private action to enforce the new tender offer disclosure laws and regulations as a necessary supplement to SEC action. . . . One obvious purpose for granting such standing is to deter future violations, and the possibility of "injunctive relief serves as a most effective weapon. . . ." The Court believes that the tender offer disclosure provisions, the anti-fraud provisions, and the SEC rules and regulations must not be violated with impunity. The Court believes "that under the circumstances here it is the duty of the courts to be alert to provide such remedies as are necessary to make effective the congressional purpose" of full and complete disclosure.\textsuperscript{51}
\end{quote}

The SEC, which filed an unsolicited amicus curiae brief in the case limited to the appropriateness of certain remedies under the Williams Act, had already instituted public proceedings against Susquehanna.\textsuperscript{52} Its order charged Susquehanna with filing a Schedule 13D containing materially misleading statements, and a hearing was scheduled for February 25, 1969. Since the alleged misrepresentations involved material required to be submitted pursuant to Section 13(d)(1)(C), the SEC was forced to consider the scope of the terms "plans or proposals" as used in that subsection. Susquehanna argued that whatever intentions it may have had concerning use of their control position within PASCO, these were merely "vague and imprecise" and therefore not to be considered "plans or proposals" within the meaning of Section 13(d)(1)(C). It also suggested that evidence of

\begin{footnotes}
\textsuperscript{48} Id. at 8.
\textsuperscript{50} Id. at 98,234.
\textsuperscript{51} Id. at 98,233-34, citing J.I. Case v. Borak, 377 U.S. 426, 432 (1964).
\end{footnotes}
corporate action or approval should have been produced, and since Korholz, while the president of Susquehanna, was neither its chief executive officer nor its largest stockholder, "[h]e cannot be said to have the power to bind the corporation on any matter by the mere oral expressions of hopes, ideas, possibilities or options . . . ."53 Finding that such arguments "fail to give adequate recognition to the purpose of the statute, to its practical aspects, and to the ingenuity of those who might wish to avoid its requirements or render it ineffectual,"54 hearing examiner Sidney Ullman found that there was no evidence indicating that any limitations or restrictions had been or were likely to be imposed upon Korholz (described as a "dominant personality within the Susquehanna organization") by the board of directors in connection with the plans which he had for the use of PASCO's cash assets. As to the contention that only those "intentions" which have reached the stage of possibly coming to fruition should and can be included in Schedule 13D as "plans or proposals," the examiner concluded that to impose upon the SEC "the burden of evaluating (and proving) the possibility of corporate management achieving the implementation of merger or acquisition intentions would in too many situations negate the language of the statute."55 Susquehanna's Schedule 13D was therefore held to contain false and misleading statements by its failure to disclose its intention to use PASCO's cash resources to make further acquisitions.

While this ruling, assuming it is upheld by the SEC, does not alter the status of Susquehanna's present stock holdings in PASCO (only an amended Schedule 13D must be filed) it is likely to influence PASCO's civil suit in the Texas District Court, and will definitely shape future conduct by prospective tender offerors. The realistic, elastic interpretation of "plans or proposals" announced by examiner Ullman strikes hard at any future attempts to thwart the full disclosure requirements of Section 13D. As stated in a committee report accompanying the Williams Bill, "[s]ecrecy in this area is inconsistent with the expectations of the people who invest in the securities of publicly held corporations and impairs public confidence in securities as a medium of investment."56

One defensive management tactic that apparently has not been tried, although there have been hints at it, is to claim that the offeror company is engaged in a fraudulent scheme by offering to pay brokers who solicit shares a double commission, which turns into a triple commission in the event the

54. Id.
55. Id. at 15.
proceeds of the tender are reinvested.\textsuperscript{57} We have seen the SEC in recent years expanding the “shingle” theory and erasing the differences between the broker when he acts as a principal and when he acts as an agent. According to the SEC, the broker in both instances owes a duty of high care to his customer.\textsuperscript{58} With this as a foundation, it seems inherently unfair to permit the offeror company to hire away through the use of the double commission the agent of the individual shareholder. One might even characterize the double commission as a “bribe.” Furthermore, I am not at all sure that placing the broker in this position can be cured by disclosure, since disclosure does not eliminate the conflict of interest inherent in the situation. Compare for example, Section 16 of the 1934 Act: Disclosure of an insider’s transactions in the shares of his corporation under Section 16(a) does not in any way lessen his liability under Section 16(b).\textsuperscript{59}

\textit{Related Areas of Change}

\textit{Access to Shareholders}

At this point in the discussion it is useful to look at what the SEC may propose with respect to shareholder lists. It seems likely that the SEC will require all offeree companies to provide shareholder lists, or send out material of the offeror company to shareholders of the offeree by virtue of a rule similar to Rule 14a-7.\textsuperscript{60} Nothing in the Act expressly provides for such a rule, but there were a number of hints during the Senate hearings that something along these lines might be adopted.\textsuperscript{61} The statutory basis for this will probably come from Section 14(d)(4).\textsuperscript{62} Under that section the SEC regulates recommendations for or against take-over bids, and I submit that it could require offeree managements to send out the opponent’s soliciting material as a condition to sending out its own material.

Before adopting a rule requiring target management to mail out the tender offer to its shareholders, the SEC should seriously examine whether this requirement should be conditioned upon the offeror agreeing not to pay double commissions to brokers who solicit for tenders. If the offerors are given access to the individual shareholders, the justification for the double commission disappears. In fact, some study should be given to the present


\textsuperscript{59} 15 U.S.C. § 78p(a), (b) (1964).

\textsuperscript{60} 17 C.F.R. § 240.14a-7 (1969).

\textsuperscript{61} \textit{Hearings on S. 510} at 169 (Stanley Reed), 176 (Manuel Cohen).

Defensive Take-over Procedures

It seems that more and more shares are being held in a street name; consequently, neither the offeror nor the offeree really has access to the individual shareholders. The SEC might, therefore, consider adopting rules requiring brokers to disclose the beneficial owners of stock held in a street name for purposes of tender offers and also for annual meetings.

**Rule 10b-6**

Rule 10b-6 under the 1934 Act should always be carefully considered if the target company or some company with which it is arranging a friendly merger proposes to bid for and purchase the stock of the target company in the open market. This rule provides, in effect, that it is a manipulative device for an issuer or an underwriter to bid for and purchase stock of such issuer if it is engaged in a distribution of such stock. The SEC's utilization of this rule was severely criticized in the *Special Study*, and the *Study* especially objected to the elastic definition the SEC has accorded the term "distribution."64

Rule 10b-6 might be operative in the take-over bid situation, irrespective of the Williams Act, in the following situations: (1) if the target company has an issue of convertible securities outstanding or if it has agreed in principle to a merger whereby it will be the surviving corporation, the SEC Division of Trading and Markets considers that the target company is engaged in a distribution and accordingly it cannot, under Rule 10b-6, bid for and purchase its own stock; and (2) if the target company arranges a merger with a friendly company, the SEC considers that the friendly company is engaged in a distribution of its own stock and that if the friendly company bids for and purchases stock of the target company it is really purchasing a right to acquire its own stock and hence is in violation of Rule 10b-6.65

Accordingly, care must be taken to examine the application of the rule in these situations and it is advisable to consult with the staff of the

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63. 17 C.F.R. § 240.10b-6 (1969).
66. As far as can be discerned, this position was only recently formalized although from experience I know that the Division of Corporate Finance has always followed it. Most securities lawyers disagreed with the position and they were supported by district court decisions in Chris-Craft Industries, Inc. v. Piper Aircraft Corp., 303 F. Supp. 191 (S.D.N.Y. 1969) and Armour & Co. v. General Host Corp., 296 F. Supp. 470 (S.D.N.Y. 1969); however, the Second Circuit, in a two to one decision, adopted the SEC's theory in the *Chris-Craft* appeal, CCH Fed. Sec. L. Rep. ¶ 92,510 (1969).

The position of the securities bar was set forth in J. FLOM, B. GARPINIEL & J. FREUND,
SEC. If there is a problem, subparagraph (f) of Rule 10b-6 provides that the SEC can upon written request or on its own motion hold that certain transactions do not fall within the ambit of the rule.

Section 13(e) Regulating Corporate Purchases of its own Registered Securities

Section 13(e) does not necessarily relate to defensive techniques, nor even to take-over bids, but it is part of the Williams Act and covers an important and expanding area of the law. The section is relatively simple and gives broad rulemaking power to the SEC. In essence, Section 13(e)(1) states that it shall be unlawful for an issuer of a class of securities registered pursuant to Section 1268 to purchase any equity security issued by it if such purchase is in contravention of such rules as the SEC may adopt in either defining acts and practices which are fraudulent or prescribing means reasonably designed to prevent such practices. The section goes on to state that the SEC’s rules may require the issuer to provide its shareholders with information relating to the reasons for the purchase, the source of funds, the number of shares to be purchased, the price to be paid for the securities, the method of purchase, and such additional information as the SEC deems necessary.

Note carefully that not only is the issuer prevented from purchasing its own securities in contravention of such rules, but Section 13(e)(2) states that for purposes of Section 13(e) “a purchase by or for the issuer or any person controlling, controlled by, or under common control with the issuer, or a purchase subject to control of the issuer or any such person, shall be deemed to be a purchase by the issuer.”

Presently, the SEC has adopted only one very narrow rule under Section 13(e). Rule 13e-1 states that an issuer may not purchase any of its equity securities while any other person is making a regulated cash tender offer for the issuer’s securities unless the issuer has filed a statement with


69. 15 U.S.C. § 78m(e)(2) (Supp. IV, 1969). This far-reaching provision received only minimal consideration during the hearings on the Williams Bill. See Kennedy, Transactions by a Corporation in its own Shares, SELECTED ARTICLES ON FEDERAL SECURITIES LAW 789, 811-12 n.11 (H. Wander & W. Grienenberger ed. 1968).
the SEC and given its security holders the substance of the information contained in the statement. The rule requires information in the statement concerning: (1) the title of the securities to be purchased, the names of the persons from whom purchased and the market in which they are to be purchased; (2) the purpose of the purchase and future plans with respect to the securities; and (3) the source and amount of funds used to make the purchase including a description of any borrowed funds.

In the future, the SEC will undoubtedly adopt detailed rules under this section. They will most likely resemble the terms the SEC was able to obtain in a consent decree in SEC v. Georgia-Pacific Corp.\(^1\) wherein the SEC charged that the defendants caused Georgia-Pacific stock to be purchased by the company and its stock bonus trust immediately prior and during the evaluation periods provided for in agreements pursuant to which Georgia-Pacific was to acquire certain other companies in exchange for its stock. The complaint also charged that the purchases were made in a manner that caused Georgia-Pacific stock to rise in order that Georgia-Pacific could issue fewer shares in connection with the acquisitions. In the consent decree, rules were established with respect to the method of purchase and also with respect to the quantity of securities that Georgia-Pacific could acquire. The SEC was also able to obtain a similar, but not identical, undertaking from Genesco in a registration statement filed by that company.\(^2\) The terms of the consent decree and the undertaking will undoubtedly be used as models for future rules in this area.

**Conclusions**

It is still too early to evaluate fully the impact of the Williams Act. It is possible, nevertheless, to draw some conclusions. The Act has not greatly enhanced the defensive abilities of target companies and has probably imposed additional hardships on them. Certainly what offeree companies say to their shareholders will be regulated, perhaps significantly, whereas it was for the most part free from regulation in the past. The Act, moreover, gives target companies no more freedom to engage in defensive tactics such as mergers and issuances of stock than they had previously. True, the anti-fraud section of the Act will most likely open the federal courts to suits brought by offeree companies against offerors, but immediately prior to the passage of the Act, the courts were starting to hear these cases. In addition, although the courts will be open to offerees, in all probability they will have less to attack since the Act and rules under the Act now establish


express disclosure requirements for offerors which are not difficult to meet and, if met, will narrowly confine the areas that offerees can criticize. Nevertheless, with the courts open and the SEC given broad regulatory power over take-over bids, target companies do have available some new tools to develop and use in combating tender offers.