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To Our Clients:

Takeovers

This outline by Mike Schwartz and Marc Wolinsky is an excellent summary of recent developments in tender offer defense.

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RECENT DEVELOPMENTS IN
TENDER OFFER DEFENSE

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Effective legal representation of a company faced with an unsolicited tender offer (a "target" company) requires careful and sophisticated meshing of litigation and corporate advice. Close coordination of these activities -- and their integration into the over-all business strategies pursued by the target -- are necessary to assure that the target's Board of Directors can participate effectively in determining the outcome of the offer.

It is the rare case in which litigation by the target can alone defeat an offer which the Board determines to oppose. However, even if litigation does not promise a "show-stopper," it is very frequently employed to bring pressure on the bidding company to improve its offer or to strengthen the target Board's position in developing a superior financial alternative. Recent developments in litigation by the target company as plaintiff are discussed in Part I below.

The target company may also find itself the defendant (or subject to a counterclaim) in litigation by the

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This outline does not consider developments involving the antitrust laws, which are being covered in a separate presentation at the panel for which this outline is being prepared.

bidder challenging corporate action by the target to compete with or oppose the unwanted bid. Complex corporate strategies of this sort have become increasingly common, as evidenced by last year's Pabst/Jacobs/Kalmanowitz, Bendix/Martin Marietta and Cities Service/Mesa battles. These developments, and others affecting litigation against the target company, are discussed in Part II below.

I. The Target Company as Plaintiff.

A wide variety of considerations may influence the target's decision whether to bring litigation, and what claims to assert. Among the kinds of claims often asserted are the following.

A. Disclosure claims.

1. Federal law: The Williams Act and SEC requirements.

a. Federal law requirements. Section 14(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and Regulation 14D promulgated thereunder, require that a person making a tender offer which will result in the offeror acquiring more than 5% of any class of stock of a company registered pursuant to Section 12 of the Exchange Act file a Schedule 14D-1 statement. A Schedule 14D-1 statement must disclose, among other things: the offeror's identity

and background; past contacts, transactions or negotiations between the target company and the offeror; the source and amount of funds for the offeror; the purpose of the tender offer and any plans or proposals the offeror may have with respect to the target; and any contract, arrangements, understandings or relationships with respect to the target's securities. The SEC also requires an offeror who is not a natural person (i.e., a corporation) to furnish adequate financial information concerning the offeror where "the bidder's financial condition is material" to the investment decision of a shareholder. The courts have extended a similar disclosure requirement to private individuals as well under appropriate circumstances, as discussed below Pursuant to Rule 14d-6(d), an offeror must "promptly" disclose any material change in the information originally disseminated.

b. Particular disclosure claims. -- Claims under the Williams Act allege inadequate or inaccurate disclosure with respect to such matters as:

-- Source and amount of funds to be used in the offer. See, e.g., Pabst Brewing Co. v. Kalmanovitz, [Current] Fed. Sec. L. Rep. (CCH) ¶ 98,873 (D. Del. 1982) (businessmen who formed corporation to make tender offer for target company, and who would personally incur

substantial indebtedness, must disclose personal net worths and other financial information); Riggs National Bank v. Allbritton, 516 F. Supp. 164 (D.D.C. 1981) (disclosure of information about financial condition of individual bidder required to enable evaluation of debt service requirements and of a loan agreement default provision that might result in the acquired shares being "liquidated"); Life Investors, Inc. v. Ago Holding, N.V., [1981-82 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,356 (8th Cir. 1981) (tender offeror required to make full financial and business disclosure notwithstanding that offer was for only 15% of target's stock and financial ability was not in issue).

-- Relationships between controlling persons and bidders. Generally, courts have been reluctant to require full disclosure of all the information required by Schedule 14D-1 with respect to controlling persons of bidders which themselves have substantial financial resources. See, e.g., Gray Drug Stores v.

Simmons, 522 F. Supp. 961 (N.D. Ohio 1981). Where the bidder does not have substantial assets or where it depends on the credit of controlling persons, such disclosure may be required. See Pabst Brewing Co. v. Kalmanovitz, supra. See also General Steel Industries, Inc. v. Walco National Corp., 527 F. Supp. 305 (E.D. Mo. 1981) (bidder, a major corporation with assets of nearly $130 million, enjoined because it did not disclose (i) the financial condition of an individual who controlled approximately 42.9% of its stock or (ii) the fact that such controlling person used the assets of the bidder for his personal and political benefit).

-- The purpose of the offer and any plans or proposals of the offeror to change the target's business or effect an extraordinary corporate transaction. See, e.g., Otis Elevator Co. v. United Technologies Corp., 405 F. Supp. 960 (S.D.N.Y. 1975) (offeror's statement in its offer that it "has not formulated any plan or proposal to merge" the target held false). Cf. Chromalloy American Corp. v. Sun Chemical

Corp., 611 F.2d 240 (8th Cir. 1979) (enjoining purchase of additional shares until Schedule 13D is amended to express adequately shareholder's intention to exert influence over the corporation's board of directors, and, through this influence, to direct the management of the company). But see Pabst Brewing Co. v. Kalmanovitz, supra (despite pattern of business practices by individuals having 50% share of offeror company, no violation found in not disclosing pattern in current offer); Crane Co. v. Harsco Corp., 509 F. Supp. 115 (D. Del. 1981) (target must show that offeror has present intention to take control, not merely likelihood that investment intention will change in future).

-- The impact on the offer of regulatory requirements, the margin regulations and the federal antitrust laws. The target can allege that failure to disclose substantive violations of any of the foregoing is itself a disclosure violation, whether or not the target has standing to assert the substantive violations themselves. See, e.g., Pabst Brewing Co. v.

Kalmanovitz, supra (allegations of non-disclosure of margin violations); Copperweld Corp. v. Imetal, 403 F. Supp. 579 (W.D. Pa. 1975) (charges of failure to disclose unlawful market manipulation under Section 9 of the Exchange Act).

2. State law: the takeover statutes.

Until the Supreme Court's decision in Edgar v. MITE Corp., 102 S. Ct. 2629 (1982), it was unclear whether the statutes regulating tender offers enacted by a great number of states were constitutional under the Commerce and Supremacy Clauses. Edgar v. MITE appears to have answered this question against their constitutionality, at least as to the Commerce Clause. The language of the opinion seems to invalidate state takeover statutes insofar as they seek to regulate open-market purchases of securities in the national securities market, and to have eliminated state law as a source of tender offer disclosure requirements (and target company claims of illegality). The Fourth Circuit in Telvest, Inc. v. Bradshaw, [Current] Fed. Sec. L. Rep. (CCH) ¶ 99,044 (4th Cir. 1983) and the Kentucky Supreme Court, in Esmark, Inc. v. Strode, 639 S.W.2d 768 (Ky. 1982) have confirmed this view. See also Martin-Marietta Corp. v. Bendix Corp., 690 F.2d 558 (6th Cir. 1982) (Michigan takeover law antifraud and Michigan

Blue Sky provisions unconstitutional as applied); Burlington Northern Inc. v. El Paso Co., Civil Action No. 82-818 (D. Del. Dec. 29, 1982) (Delaware provision requiring extended proration period unconstitutional where then applicable SEC rule gives bidder flexibility in closing period); Mesa Petroleum Co. v. Cities Service Co., [Current] Fed. Sec. L. Rep. (CCH) ¶ 99,064 (W.D. Okla. 1982) (Oklahoma act unconstitutional even if construed to apply solely to purchases of shares from Oklahoma residents).

Edgar v. MITE would also seem to have ended the practice of requiring state law hearings concerning the adequacy of disclosure, and thus to have the effect of eliminating an alternative forum formerly available to targets. The state of Ohio, whose previous statute had provided for such hearings, has recently enacted a new takeover statute, applicable to Ohio corporations with principal places of business, principal executive offices or substantial assets within Ohio, which purports to regulate the internal affairs of the corporation, a traditional area of state regulation, and without at least some of the features found offensive in Edgar v. MITE. The statute requires shareholder votes on "control acquisitions" of shares, as defined. Ohio Rev. Code § 1701.831.

However, Ohio's new statute, like its predecessors, purports to be extraterritorial in its reach and imposes major

delays on covered transactions. It would preclude tender offerors from purchasing shares in accordance with the time periods set forth in Section 14(d) of the Exchange Act and SEC Regulation 14D thereunder. Accordingly, despite the fact that the statute apparently regulates internal affairs, there is still an issue as to the statute's enforceability under the Commerce and Supremacy Clauses.

B. Other federal and state laws regulating changes of control.

In addition to the Williams Act and state takeover statutes, numerous federal and state statutes regulate the change in control of corporations engaged in certain regulated businesses, by tender offer or other means. These may also form the basis for litigation claims by the target company.

1. Federal law.

a. "Change in control" statutes. -- Certain federal regulatory statutes require administrative agency approval prior to consummation of a change in control of a regulated target. *See, e.g.*, the Federal Communications Act, 47 U.S.C. § 310; the Interstate Commerce Act, 49 U.S.C. § 11343; the Federal Aviation Act, 49 U.S.C. § 1378; the Bank Holding Company Act, 12 U.S.C. § 1842; the Change in Bank

Control Act, 12 U.S.C. § 1817(j). These regulatory statutes typically provide that the acquisition of a certain percentage of the target's securities is deemed to constitute a change of control.

b. Private right of action. -- Some of these statutes may be used by the target to seek a preliminary injunction in federal court. Several courts have found that a target bank has standing to bring a private action to enjoin violations of the Change in Bank Control Act, supra. See First Alabama Bancshares, Inc. v. Lowder, [1981 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,015 (N.D. Ala. 1981); Mid-Continent Bancshares, Inc. v. O'Brien, [1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,734 (E.D. Mo. 1981). But see Flagship Banks, Inc. v. Smathers, 81-713-Civ.-EPS (S.D. Fla. July 22, 1981). Several courts have refused to find a private cause of action under the Bank Holding Company Act. See First Alabama Bancshares, supra; Flagship Banks, supra. See also Financial Corporation of Santa Barbara v. Dayco Corp., No. CV 80-2919-RJK (C.D. Cal. Sept. 25, 1980) (no private right of action under Federal Change in Savings and Loan Control Act, 12 U.S.C. § 1730(q)).

Whether or not a private cause of action exists, failure to properly disclose the applicability and/or impact of change in control statutes may constitute a disclosure

violation under the Williams Act, *supra*. *See, e.g.*, *Riggs National Bank* v. *Allbritton*, 516 F. Supp. 164 (D.D.C. 1981).

Moreover, the target company may challenge the bidder's non-compliance with the approval requirement before the agency itself. For example, in the recent Continental Airlines/Texas International Airlines matter, Continental contested (unsuccessfully) the decision of the Civil Aeronautics Board to permit Texas International to acquire up to 48.5 percent of the voting stock of Continental prior to the grant of approval under Section 408 of the Federal Aviation Act (which contains a rebuttable presumption that ownership of ten percent or more of the voting stock constitutes control) provided such holdings were placed in a voting trust. CAB Order 81-13-130 (March 3, 1981). The trust was structured to require proportionate voting of the shares held in trust but permitted Texas International to vote such shares against Continental's proposed merger with Western Air Lines.

2. *State law*.

Certain state statutes, such as insurance holding company laws, *e.g.*, Mo. Rev. Stat. § 382.040, or bank holding company laws, *e.g.*, N.Y. Banking Law § 142, prohibit the acquisition of control of an insurance company or state-

chartered bank unless the appropriate state agency has approved the transaction, and may prevent the commencement of a tender offer without regulatory approval. The decision in Edgar v. MITE Corp. leaves open the question of whether such statutes are constitutional. In John Alden Life Ins. Co. v. Woods, [1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,617 (D. Idaho 1981), and in Professional Investors Life Ins. Co. v. Roussel, 528 F. Supp. 391 (D. Kan. 1981), certain provisions of state insurance holding company statutes were upheld in the face of attacks on their constitutionality, while in National City Lines, Inc. v. LLC Corp., 524 F. Supp. 906 (W.D. Mo. 1981), aff'd on other grounds, 687 F.2d 1122 (8th Cir. 1982), and Gunter v. Ago International B.V., 533 F. Supp. 86 (N.D. Fla. 1981), similar provisions were struck down on the ground that they were preempted by the Williams Act.

C. Federal margin regulations.

1. The regulatory framework.

Pursuant to Section 7(f) of the Exchange Act, 15 U.S.C. § 78g(f), the Federal Reserve Board has adopted regulations governing the use of bank credit in purchasing stock. Regulation X (12 C.F.R. § 224) prohibits a borrower from obtaining credit secured directly or indirectly by "margin

securities" (as defined in 12 C.F.R. § 221.3(v)) for the purpose of purchasing or carrying that stock in an amount exceeding the "maximum loan value" of the stock. Similarly, Regulation U (12 C.F.R. § 221) prohibits a bank from extending credit in excess of the "maximum loan value." The Federal Reserve Board has defined the "maximum loan value" of margin stock to be "50 percent of its current market value, as determined by any reasonable method." Supplement to Regulation U, 12 C.F.R. § 221.4(a). One court has held that, for purposes of the margin regulations, a target company's stock may "reasonably" be valued at the tender offer price, even if the offer is for less than 50% of the stock. _Pabst Brewing Co. v. Kalmanovitz_, _supra_.

2. _Private right of action_.

The courts are split over whether a target company has standing to seek to enjoin the purchase of its stock where the purchase would be financed in violation of the margin regulations.

a. Three courts have found that there is a private right of action: _Pabst Brewing Co._ v. _Jacobs_, [Current] Fed. Sec. L. Rep. (CCH) ¶ 99,042 (D. Minn. 1982); _Pargas, Inc._ v. _Empire Gas Corp._, 423 F. Supp. 199, 241-42 (D. Md.), _aff'd_, 546 F.2d 25 (4th Cir. 1976); _Metro-Goldwyn-Mayer, Inc._ v. _Transamerica Corp._, 303 F. Supp. 1354 (S.D.N.Y. 1969).

b. Three courts have refused to find a private cause of action in a target company: First Alabama Bancshares, Inc. v. Lowder, [1981 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,015 (N.D. Ala. 1981); D-Z Investment Co. v. Holloway, [1974-1975 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,771, at 96,562 (S.D.N.Y. 1974); Nachman Corp. v. Halfred, [1973-1974 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,455 (N.D. Ill. 1973). Cf. Walck v. American Stock Exchange, Inc., 687 F.2d 778 (3d Cir. 1982) (no private right of action in favor of an investor for violations of the margin requirements).

D. RICO.

A new, and highly controversial, device for combatting takeover attempts which has developed involves the use of the Racketeer Influenced and Corrupt Organizatons Act, 18 U.S.C. §§ 1961-68 ("RICO").

1. Provisions of the act.

Section 1962 of RICO prohibits:

> (a) the use of "any income derived, directly or indirectly, from a pattern of racketeering activity" to acquire an interest in any enterprise that is engaged in or affects interstate or foreign commerce (there is an exemption for open market purchases of securities for investment and not for control if the total number of shares held after the purchases do not amount to one percent of the outstanding shares of any one class and do not confer, in law or in fact, the power to elect one or more directors);

> (b) the use of a "pattern of racketeering activity . . . to acquire or maintain, directly or indirectly," any interest in such an enterprise;
>
> (c) any employee of such an enterprise from conducting its affairs "through a pattern of racketeering activity."

Section 1962(d) also makes it unlawful for any person to conspire to violate subsections (a), (b) or (c). Section 1961(5) defines "pattern of racketeering activity" as "at least two acts of racketeering activity . . . the last of which has occurred within ten years . . . after the commission of a prior act of racketeering activity." Section 1961(1)(D) defines "racketeering activity" to include "any offense involving . . . fraud in the sale of securities." Section 1964(a) gives District Courts "jurisdiction to prevent and restrain violations of Section 1962 . . . by issuing appropriate orders," including divestiture and dissolution.

2. Viability of a RICO claim by a target <u>company - the Dan River case.</u>

The Fourth Circuit's recent decision in <u>Dan River, Inc.</u> v. <u>Icahn</u>, [Current] Fed. Sec. L. Rep. (CCH) ¶ 99,043 (4th Cir. 1983) puts the viability of a RICO claim in all but the most unusual tender offers (<u>i.e.</u>, where Murder, Inc. is the raider) in doubt. In <u>Dan River</u>, the target sued Carl Icahn and several Icahn companies alleging, among other things, a claim under RICO. Dan River alleged that Icahn had

committed mail and securities frauds through the improper use of Bayswater, a company he controlled, and through his so-called "buy-me-out-or-face-a-takeover" investment tactics.

Reversing the District Court's grant of a preliminary injunction against Icahn's partial tender offer, the Fourth Circuit expressly found that Dan River had not shown a substantial likelihood of success on the merits of its RICO claim and, ultimately, probably could not prove its claim. As the Court stated, "it would seem extremely unlikely that Dan River will be able to prove the predicate acts of mail or securities fraud." Id. at 94,964. The Court also noted that it was doubtful whether RICO was even applicable to the type of activity challenged by the plaintiff. As the Court stated, in enacting RICO, "Congress was out to attack the problem of organized crime, not the problems of corporate control and risk arbitrage." Id. See also Marshall Field & Co. v. Icahn, 537 F. Supp. 413 (S.D.N.Y. 1982). But see Spencer Companies, Inc. v. Agency Rent-A-Car, Inc., [1981-82 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,361 (D. Mass. 1981) (allegations that an acquiring company had filed a series of misleading Schedule 13D statements in violation of Section 13(d) of the Exchange Act stated a "pattern of racketeering activity" as that term is used in RICO).

II. Corporate Defense Strategies and the Target Company as Defendant.

A. Introduction.

Because of the increasing difficulty of fending off a hostile bidder with legal defenses, the recent wave of tender offers has re-emphasized the need for a target to find corporate and financial alternatives to an unwanted bid. Typically, a target company will seek out a competing bidder or "white knight," often facilitating the white knight's success with any one of a variety of devices. *See* II.B., *infra*. A second alternative is for the target to adopt one of the so-called "disaggregation defenses," *e.g.*, selling off attractive assets or engaging in an issuer self-tender offer. *See* II.C., *infra*. Other strategies include the making of a counter-tender offer for the bidder (the so-called "Pac-man" defense), *see* II.D., *infra*, issuing shares of the target's own stock, either to friendly hands or to its existing shareholders, *see* II.E., *infra*, or adopting defensive by-law provisions, *see* II.F., *infra*. In defending against a tender offer, a target may also, within strictly defined parameters, influence the outcome by influencing shares held by employee stock ownership plans. *See* II.G., *infra*. As explained below, adoption of these approaches has increasingly involved target companies in litigation initiated by the original bidder. *See* II.H., *infra*.

These corporate strategies are sometimes used in complex combinations. For example, in the recent Pabst/ Jacobs/Kalmanovitz matter,* Pabst -- the target of an unwanted bid by a company controlled by Irwin Jacobs and Paul Kalmanovitz -- found a "white knight" in the G. Heileman Brewing Co., and agreed that Heileman would make a tender offer for Pabst shares at a price acceptable to the Pabst Board, following which Heileman would retain certain assets which it desired and, in effect, "spin off" the remaining assets to the shareholders, leaving a free-standing Pabst as an independent company. This plan -- which had elements of the white knight defense, "disaggregation," and the issuance of shares into friendly hands -- was successful in defeating the unwanted Jacobs/ Kalmanovitz tender offer and in ending a year of corporate warfare between Pabst and Jacobs.

B. "White knight" defense.

For several years, the most common strategy for a target of an unsolicited takeover attempt has been to search for an alternative buyer of its choice, a "white knight."

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* The authors' firm was counsel to Pabst in this matter.

1. Lock-up agreements - general.

Should the target opt for the white knight strategy, various devices, known collectively as "lock-ups," may be employed to make consummation of the transaction more certain. A lock-up has the advantages to the target of encouraging bidders who might otherwise be unwilling to participate in an auction of the company, and discouraging potential or actual hostile bidders from disrupting the transaction. However, its use is by no means to be recommended routinely.

2. Forms of lock-ups.

a. Stock purchase agreements. -- The target may sell the friendly offeror preferred stock with special voting rights. While this lock-up greatly deters hostile bids, it is vulnerable to the attack that it artificially "manipulates" the market for target stock. See Mobil Corp. v. Marathon Oil Co., 669 F.2d 366 (6th Cir. 1981) (discussed below). The issuance of preferred stock with special voting rights by a corporation's board of directors may also be subject to attack on the grounds that voting rights are being manipulated without shareholder approval. See Telvest v. Olson, Civ. No. 5798 (Del. Ch. March 8, 1979) (discussed below). Consideration should also be given to stock exchange rules which prohibit the acquisition of more than specified percentages (18.5%

in the case of the New York Stock Exchange) of a company's stock without shareholder approval.

b. Stock options. -- The flexibility inherent in the option contract has accounted for the recent popularity of this form of lock-up. The granting and exercise of lock-up options are subject to the same legal constraints discussed below with respect to stock purchase agreements.

c. "Crown jewel" options. -- These are useful only where the target has a "crown jewel" which is the raison d'etre for acquiring the target -- e.g., Marathon's Yates field. It should be kept in mind that agreements to sell major assets at low prices could give rise to fiduciary claims, and that, after Mobil Corp. v. Marathon Oil Co., supra, these options are vulnerable to claims of manipulation. But see Whittaker Corp. v. Edgar, 535 F. Supp. 933 (N.D. Ill. 1982) and Marshall Field & Co. v. Icahn, 537 F. Supp. 413 (S.D.N.Y. 1982), discussed infra.

C. Disaggregation defenses.

1. General.

A more extreme response to a potential or actual hostile takeover attempt is for the target company to propose a substantial restructuring of itself through the sale of

divisions, partial liquidations, spin-offs, self-tender and the like, referred to collectively as "disaggregation" transactions. These defensive maneuvers usually come under consideration where the target believes that its stock price does not adequately reflect underlying asset values. Defensive disaggregation transactions (with the exception of a simple sale of target assets where the sale proceeds are not distributed to shareholders) offer target company shareholders an alternative to the tender offer: for the defense to succeed, shareholders must determine that the target's proposed actions will provide greater financial returns than the raider's offer. In proposing a disaggregation transaction, the target is in effect making a competing offer to its shareholders, which they are free to accept or reject.

2. Types of disaggregation defenses.

a. Sale of attractive or undervalued assets. -- A target may be able to make an unsolicited bidder drop its offer by selling off those assets which are most attractive to the raider. For example, in Whittaker's recent bid for Brunswick, it was thought that Whittaker's bid was motivated in large part by its desire to acquire Brunswick's medical group (one of a few separate business segments of Brunswick). While the Whittaker bid was pending, Brunswick entered into an agreement with American Home Products for the latter's

acquisition of that division. Following the Seventh Circuit's affirmance of the lower court's denial of the preliminary injunction sought by Whittaker, Whittaker terminated its offer and 98% of Brunswick's stock was tendered to American Home Products.

Even if a sale can be arranged, however, this strategy may not necessarily be successful. In Grand Metropolitan's bid for Liggett Group, it was thought that Grand Met's bid was motivated in large part by its desire to acquire Liggett's Austin Nichols subsidiary (because of the distribution network Austin Nichols could provide in the United States for Grand Met's products). While the Grand Met offer was pending, Liggett sold Austin Nichols to Pernod Ricard S.A. in an effort to make Liggett less attractive to Grand Met. Grand Met did not withdraw its bid, however, although it did raise its price to stop Standard Brands' "white knight" bid for Liggett.

If the sale of assets fails to force the bidder to withdraw of its own accord, the target may use the proceeds of the asset sale to acquire a business which poses antitrust or regulatory problems for the bidder or to finance a self-tender offer which substantially reduces the target's capitalization and/or raises the percentage held by major shareholders who support target management. In addition to

depriving the raider of the assets, another effect of an asset sales is to reduce the bidder's ability to finance its offer through its sale of such assets after the acquisition. However, a large bidder may not be deterred by such sales if it is determined to acquire the target, and a reduction in the target's capitalization could make it easier for the raider to make the acquisition. In addition, the target may be unable to realize top dollar on the assets sold because of the pressure to sell quickly.

b. Partial liquidation. -- A target with undervalued assets can sell off assets and distribute the proceeds to shareholders. This alternative provides both an immediate cash return to shareholders and the opportunity for investors to remain as shareholders in the ongoing business concern. In addition, it deprives the bidder of the benefits of the assets sold and gives the target an opportunity to demonstrate to its shareholders that the company's value is greater than the tender offer price. On the negative side, in addition to the factors discussed above with respect to any sale of assets, the market will discount the value of the partial liquidation by the time required to consummate the transaction and the uncertainties associated with achieving the promised values. (These two problems may be handled by combining the partial liquidation with a spin-off, discussed below.)

c. Spin-off. -- A variant of the partial liquidation is a spin-off by a target of an undervalued asset group either directly, by distributing the shares of a subsidiary to shareholders, or indirectly, by transferring the assets into a separate entity such as a trust, partnership, or other corporation, the shares or interests in which are then distributed to the target's shareholders. In contrast to the partial liquidation, in which shareholders receive one or more lump-sum payments, a spin-off provides shareholders with a continuing source of income from the undervalued assets. As with the partial liquidation, the target company remains independent.

Examples of spin-offs include: (i) Mesa Petroleum's two spin-offs of oil and gas properties, see Mesa's Proxy Statements, dated September 21, 1979 and November 10, 1982; (ii) Metro-Goldwyn-Mayer Inc.'s spin-off of film operations, see MGM Proxy Statement, dated May 2, 1980; (iii) Engelhard Minerals' spin-off of minerals and chemical divisions, see Engelhard Proxy Statement, dated April 22, 1981; and (iv) Wheelabrator-Frye's spin-off of shares of Pullman Transportation Company, see Pullman Prospectus, dated February 12, 1982.

d. Total liquidation. -- If a target's Board, upon consultation with its investment bankers, believes that the company's individual assets have liquidation values in

excess of the price the bidder is offering, the target may attempt to realize those higher values by proposing to liquidate the target at a per share price above the offer. As in the case of a partial liquidation, the liquidation value of the target must not only be greater than the offer price, but high enough to offset the discount that will result from the time necessary to effect the liquidation and the uncertainty in achieving the values promised. (Such discount will be smallest when the asset values of the company can relatively easily be established, _i.e._, when the company has "hard" assets such as oil and gas reserves or real estate.)

Target management must of course be prepared to carry through with the proposal even if the bidder goes away, which makes the total liquidation alternative unacceptable for many targets. Another problem with total liquidation is that it places a price on the company, which makes it very difficult to resist a bidder which comes in at a higher price (or the original bidder, if it raises its offering price above the announced liquidation value). However, as noted above, total liquidation can be proposed for just that purpose: to force a bidder to raise its initial offer or to attract another bidder at a price equal to or greater than the proposed liquidation price.

e. _Self-tender - General American_. -- A target may make a competing offer by offering to purchase a portion

of its own shares for cash at a price substantially in excess of the bidder's price. This option has the advantage of affording shareholders the choice of obtaining cash pursuant to the self-tender or remaining shareholders in a company which target management believes will provide higher returns over time.

One problem with using this approach as a response to an any-and-all cash tender offer is that target shareholders may be unwilling to risk proration of their shares even at the higher price offered by target; moreover, if target shareholders are unimpressed by management's expectation of the target's future earnings potential, they will be unwilling to stay with the target when faced with the prospect of receiving cash immediately for all their shares from the bidder.

This device was recently employed by General American Oil in response to a tender offer by Mesa Petroleum. Mesa offered $40 per share for 50% of General American Oil and stated its intention to acquire the other 50% for Mesa securities worth less than $40 per share. General American, being debt-free, arranged a $600,000,000 loan to finance a self-tender at $50 per share and, after making the self-tender, dropped all but the "white knight" condition to its self-tender -- so that if Mesa obtained 50% of General

American at $40 per share, General American would purchase a major portion of the balance at $50 per share and thereby provide a cash "second step," giving General American shareholders an average price of $45. Ultimately Phillips Petroleum Co. came in as a white knight at an average price of $45 per share and the General American self-tender provided convenient financing for Phillips as well as the assurance of success it sought as a condition to making its bid. Thus, the self-tender proved to be a means both of protecting target shareholders against a "second-step" for paper of uncertain (but lower) value than the "front-end" tender offer and a means of facilitating a "white knight" transaction. However, it should be noted that a self-tender of this magnitude is possible only in the rare case where the target has sufficient unrestricted assets to support borrowing to repurchase almost 50% of its stock.

D. Counter-tender offers.

1. General.

Counter-tender offers have become an accepted offensive and defensive strategy in the past year. NLT-American General showed the efficacy of the counter-tender offer to obtain a higher price. The Cities Service bid for Mesa Petroleum illustrated the benefits of a preemptive strike. The

Olympia Brewing counter offer for Pabst, made at a time when Olympia was 49% owned by Pabst, was designed both to defeat a competing offer and to effect a planned recapitalization. Heublein's counter purchase of General Cinema stock caused General Cinema to repurchase its stock in order to concentrate General Cinema's percentage of control and thereby diverted General Cinema from acquiring more Heublein stock.

By making a counter-tender offer, the target necessarily waives certain defenses such as antitrust and regulatory claims and implicitly acquiesces in the desirability of a business combination (although only on its terms).

2. Bendix-Martin Marietta.

The most noted counter-tender offer of the past year, Martin Marietta's counter-tender offer for Bendix, highlighted the difficulty and delicate balancing involved in turning a counter-tender offer into a successful defense strategy. A key to Martin Marietta's ability to utilize the counter-tender offer was a fortuitous difference between Delaware and Maryland law. In its offer for Bendix (a Delaware corporation) Martin Marietta (a Maryland corporation) stated that upon acquiring more than 50% of the voting power of Bendix, pursuant to Section 228 of the Delaware General Corporation Law, Martin Marietta, acting by written

consent and without a meeting of stockholders, expected to adopt resolutions designed to assure its control of Bendix. Even though Bendix owned more than 50% of Martin Marietta, the Delaware consent procedure would have permitted Martin Marietta to exercise control over Bendix before Bendix could exercise control of Martin Marietta under Maryland law, which does not have a comparable provision. While SEC Rule 14c-2 requires that shareholders be provided a written information statement 20 days prior to the taking of action by written consent, this rule can be complied with by including the requisite information in the tender offer documents, as was done by Martin Marietta. In light of Bendix-Martin Marietta, companies should carefully analyze their charters in advance of a takeover. A Delaware company should consider amending its charter to eliminate the ability of a majority shareholder to act by written consent. Corporations organized in other states should review the law applicable to them and focus on the consent mechanism applicable in their state.

A second novel issue raised, but not answered, by Bendix-Martin Marietta involves the question of "double subsidiaries" -- whether the target may vote stock of the bidder if each owns a majority of the other. Section 160(c) of the Delaware General Corporation Law provides that a subsidiary may not vote stock of its parent that it owns. In order to

obtain a decision from the Delaware Court so as to be able to purchase the Bendix shares promptly, Martin Marietta volunteered not to vote the Bendix shares if the Court did not enjoin the purchase. The Court enjoined voting, but permitted the purchase even though Bendix already owned 70% of Martin Marietta.

While the Delaware Supreme Court previously had said that if Martin Marietta were to purchase Bendix shares and seek to replace the Bendix Board by written consent at a time when Bendix was the majority shareholder of Martin Marietta it would do so "in violation of a moral duty to its majority shareholder", this statement was made in the context of the Court's finding that the Chancery Court did not abuse its discretion in declining to enjoin the Bendix shareholder meeting. Martin Marietta Corp. v. Bendix Corp., No. 298 (Del. Supr. Sept. 21, 1982). If the contest had not been resolved when it was, there likely would have been extensive litigation on the issue of the ability of Bendix and Martin Marietta to exercise control over each other.

E. Issuing shares.

Several target companies have sought to defend against tender offers by issuing shares of authorized but unissued stock to friendly hands and, in at least two cases, to their existing shareholders.

1. Placing a block in friendly hands.

Generally, shares may be issued for the purpose of defeating a takeover if the target properly determines that the takeover is not in the best interest of the shareholders or if such issuance is not for the sole or primary purpose of perpetuating management. Where an independent business purpose does exist, the transaction may also be motivated by a desire to defeat an unwanted takeover. Moreover, in certain situations where the proposed takeover itself may appropriately be viewed as injurious to the best interests of the corporation and its stockholders, that circumstance alone may provide the legitimate business purpose to justify defensive tactics.

a. Specific examples. -- (i) In the Dan River/Icahn situation, Dan River created a new series of voting preferred shares and made them available only to its employees under the company's profit-sharing plan. The preferred shares would have a class vote on any proposed merger if a person or group owned more than 35% of the company's common stock.

(ii) In a recent proxy contest, the issuance of 3.25 million shares of authorized but unissued shares by Global Natural Resources PLC in a merger with a

private company was challenged by an insurgent on the grounds that the transaction was dilutive and violated Section 10(b) and state law fiduciary duties. The Sixth Circuit denied relief. Warner v. Global Natural Resources PLC, Nos. 82-3538, 82-3546 (6th Cir. Sept. 3, 1982).

(iii) In Consolidated Amusement Co. v. Rugoff, [1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,584 (S.D.N.Y. 1978), the Court held that corporate management is not entitled to take steps to block an unwanted takeover, such as placing a block of stock in "friendly" hands, where there is no independent legitimate business purpose to the transaction. The case, however, presented particularly aggravated circumstances, including the "parking" of the stock (i.e., placing it in friendly hands with agreement such that the holder had no financial interest and incurred no downside risk), the absence of investment bankers' advice, the acceptance of inadequate consideration and the making of false statements as to the purported reasons for the transaction.

b. Special considerations for NYSE companies. -- A target company listed on the NYSE must keep in mind that issuance of a large block may result in delisting. The NYSE's so-called 20% Rule restricts the ability of a corporation to

issue securities without shareholder approval where such issuance involves a "change of control" or the acquisition of a business. For example, in May 1981, Continental Airlines filed a listing application with the NYSE to list an additional 15.4 million shares of its common stock, which Continental planned to issue to the Continental Employee Stock Ownership Trust ("ESOT"). As a result of the transaction, the ESOT would hold approximately 51% of the total number of outstanding shares.

Texas International Airlines, which owned approximately 48.5% of the currently oustanding shares of Continental common stock (acquired in a hostile tender offer), challenged the transaction. If the the new shares were issued to the ESOT, Texas International's holdings would have dropped to about 24% of the outstanding shares and the percentage of the outstanding shares held by the public would have dropped to approximately 25%. In June 1981, the NYSE ruled that Continental was required to seek shareholder approval as a condition for listing the additional shares on the NYSE (on the basis that the proposed transaction involved a change in control of Continental even though the ESOT shares would be voted by the Continental employees) and to obtain approval of over 50% of holders of the outstanding common stock of Continental. The NYSE further stated that if the shares were issued to the

ESOT without the prior approval of the shareholders, the NYSE would delist the common stock of Continental.

2. Issuing shares to the target's own shareholders.

In two cases, target companies have sought to issue preferred stock to their existing common shareholders, giving the preferred stock class voting rights designed, in varying degrees, to impede the objectives of the raider. Such a defense is available only to companies whose certificate of incorporation authorizes the Board of Directors to issue preferred stock with special class voting rights.

a. Telvest. -- In Telvest v. Olson, Civil Action No. 5798 (Del. Ch. March 8, 1979), the target sought to issue "preferred" stock to its existing common shareholders as a dividend pursuant to blanket authority contained in its certificate of incorporation. The Court invalidated the action, finding that the stock was not truly "preferred" since the only preference the stock had was a super-majority class vote as to business combinations with a 20% stockholder. The Court concluded that by issuing the stock, Telvest's Board was trying to alter the voting rights of the target's common stock, something which it found to be impermissible under Delaware law.

b. El Paso. -- The El Paso Company attempted a similar but, it hoped, distinguishable defense in response to Burlington Northern's recent $24 per share offer for 50% of El Paso's common stock. Burlington Northern had stated its intention not to acquire the balance of the shares in the foreseeable future but to take control of El Paso and thereafter decide what (if anything) it might propose for a second step. El Paso is highly leveraged and while it determined to seek a "white knight", it was recognized that it could be difficult to find one. El Paso had authorized "blank check" preferred stock. In order to provide some protection to the El Paso shareholders, El Paso created a series of convertible preferred stock and declared a dividend of one share for each 20 shares of common.

Unlike the stock in Telvest, El Paso's preferred had all the incidents of true preferred stock: it was convertible share for share into common, was noncallable for five years and had a fixed dividend and liquidation preference. It also contained special protection for the El Paso shareholders upon Burlington Northern obtaining control of El Paso. The preferred provided for a class vote for one-third of the directors if Burlington Northern did not propose a "fair" second step within 10 days. Approval of either (a) 90% of the preferred shares voting as a class, other than

those held by Burlington Northern, or (b) a majority of the "remaining" El Paso directors, essentially those not elected by Burlington Northern, was required if Burlington Northern attempted a second step other than for cash at the first step price. Thus, unlike the preferred stock in Telvest, El Paso's preferred was designed to protect El Paso's remaining shareholders in any second-step transaction; it was not designed to prevent the raider from acquiring shares.

Burlington Northern attacked the legality of the preferred stock dividend. See Complaint, Burlington Northern Inc. v. El Paso Co., Civil Action No. 7050 (Del. Ch. 1982). Before the case was decided, the parties reached an agreement.

F. Defensive by-law provisions.

By-law provisions designed to restrict the transferability of shares have met with limited success in tender offer defenses.

1. REITs.

In response to a tender offer by APC Investments, the trustees of Pacific Realty, a real estate investment trust, enacted a by-law provision prohibiting any shareholder from owning more than 9.8% of the stock of the target company in an attempt to protect the trust's tax status. An Oregon

trial court held that the by-law was valid, but refused to enjoin the offer. However, the United States District Court for the District of Oregon permanently enjoined APC from proceeding with the offer, finding that the by-law would prevent consummation of the offer. In Pacific Realty Trust v. APC Investments, Inc., 685 F.2d 1083 (9th Cir. 1982), the Ninth Circuit, reversing the District Court, held that the Williams Act did not prohibit the making and consummation of a tender offer in the face of the by-law. Although remanding the case to the District Court for a review of the adequacy of the disclosure, the Court of Appeals determined that adequate disclosure was the protection afforded shareholders in this situation by the Williams Act, and that it was "far from certain that APC cannot complete the proposed offer lawfully." Subsequent to the federal decision, the Oregon Court of Appeals held the by-law provision invalid. See Pacific Realty Trust v. APC Investments, Inc., 59 Or. App. 425, 651 P.2d 163 (1982).

In San Francisco Real Estate Investors v. Real Estate Investment Trust of America, No. 82-3284-MA (D. Mass. November 17, 1982), the Court held that management of a REIT acted in "good faith" and for a proper business purpose when it adopted a restrictive by-law providing that no person shall vote or receive dividends on shares owned in excess of 9.8 percent of its outstanding shares. The Court held that such by-law was not a "manipulative device" under Section

14(e) of the Exchange Act. Rejecting the contention that the by-law was invalid because it breached the explicit terms of the trust's charter, the Court held that "even if those breaches were shown it would not affect any conclusion that the trustees acted in good faith . . . ."

2. Seagram-Conoco.

In Joseph E. Seagram & Sons, Inc. v. Conoco, Inc., 519 Supp. 506 (D. Del. 1981), the Court was faced with a by-law provision that restricted the transfer of stock ownership to aliens which, if enforced, would have foreclosed Seagram's tender offer for Conoco shares. The ostensible purpose of the provision was to insure that federal and state laws restricting the activities of corporations owned in whole or part by aliens would not hinder Conoco from conducting its business.

The Court held the restrictive by-law invalid but side-stepped the issue of whether the by-law itself was "manifestly unreasonable" and therefore not permitted by Delaware G.C.L. § 202(c)(4). Rather, the Court relied on a provision of the Delaware law, Delaware G.C.L. § 202(b), that requires that any restriction on the transferability of securities imposed after the issuance of the securities be subject to the consent of the holder of such securities, either pursuant to an agreement of the holder or a vote in favor of the restriction.

G. Employee stock ownership plans.

In many cases, a target's largest shareholder will be the trustee of its employee stock ownership plan. Especially where a partial tender offer has been made, the ultimate disposition of shares held in such plans may influence the ultimate outcome of the takeover. Two recent decisions illustrate the importance of reviewing employee benefit plans to assure that the proper mechanisms with respect to voting and tendering shares are in place prior to a tender offer. Unless the plan provides that employees are entitled to vote the shares and instruct the trustee as to the tender of the shares, it may be difficult to avoid an adverse result. Whatever steps the target takes, however, target management must be scrupulously careful to observe any independent fiduciary obligations owed to plan members. See Donovan v. Bierwirth, 538 F. Supp. 463 (E.D.N.Y. 1981), aff'd, 680 F.2d 263 (2d Cir. 1982).

1. Bendix.

In response to Martin Marietta's counter-tender offer for Bendix stock, Citibank, as trustee of a Bendix employee plan, tendered all the Bendix stock in the plan to Martin Marietta. The federal District Court in New York, in a decision affirmed by the Second Circuit, prohibited Citi-

bank from following the directions of Bendix management to withdraw the Bendix stock unless instructed to tender by the employees. Martin Marietta Corp. v. Bendix Corp., 82 Civ. 6135 (S.D.N.Y. 1982), aff'd, [Current] Fed. Sec. L. Rep. (CCH) ¶ 99,067 (2d Cir. 1982). While the employees had the right to vote the shares in the plan, the plan was silent on the issue of tendering shares (except to the extent it permitted withdrawal by an employee of his shares at the end of a month) and the Court concluded that the trustee was obligated to tender to Martin Marietta unless instructed to the contrary by the employees. Ultimately, after a major effort to reach plan members, Citibank received instructions with respect to 94% of the Bendix plan shares. Almost all of the plan members elected not to tender. See Martin Marietta Corp. v. Bendix Corp., [Current] Fed. Sec. L. Rep. (CCH) ¶ 99,068 (S.D.N.Y. 1982).

2. El Paso.

Citibank was faced with the same dilemma in the recent Burlington Northern tender offer for El Paso. This time, however, El Paso's Board of Directors, in consultation with Citibank, amended El Paso's employee stock ownership plans to provide that Citibank tender a plan member's El Paso stock to Burlington Northern only if it received directions to do so. El Paso's management mounted an all-out effort to contact

plan members, provide them with the offering materials and obtain instructions from them as to whether they wanted to tender prior to the proration date. Burlington Northern failed in its attempt to obtain a temporary injunction like the one issued in Martin Marietta v. Bendix, supra, directing the trustees to tender the plan stock prior to the proration date, see El Paso Co. v. Burlington Northern, Inc., Civil Action No. E.P. 82-C.A. 397, largely because by the time Burlington Northern's motion was heard, well over 90% of the El Paso plan members had communicated their personal investment decision to the plans' trustees.

H. The target company as defendant.

As target companies have with increasing frequency resorted to corporate responses to tender offers, they have also found themselves defending their actions against legal attack by the bidder. Allegations that the target's directors violated their fiduciary duties have generally been unsuccessful. Attacks based on alleged violations of Section 14(e) of the Exchange Act which prohibits market manipulation in connection with tender offers have met with limited success.

1. The business judgment rule applies to and normally protects the actions of directors in structuring defenses.

Recent federal decisions construing Delaware, New York, Maryland and general corporate law affirm the proposi-

tion that directors are entitled to the protection of the business judgment rule when responding to hostile takeover bids as long as the directors act in good faith and a rational business purpose can be attributed to their decision. See, e.g., Panter v. Marshall Field, 646 F.2d 271 (7th Cir.), cert. denied, 454 U.S. 1092 (1981); Treadway Companies v. Care Corp., 638 F.2d 357 (2d Cir. 1981); Johnson v. Trueblood, 629 F.2d 287 (3d Cir. 1980), cert. denied, 450 U.S. 999 (1981). Increasingly, the federal and state courts have indicated that they will exercise restraint and not permit themselves to tip the balance in favor of one participant or the other. See, e.g., Martin Marietta Corp. v. Bendix Corp., 547 F. Supp. 533 (D. Md. 1982). These cases make clear that numerous defensive actions -- including, inter alia, counter-tender offers, sales of the target's assets, purchases of the company's own stock, placements of a block in friendly hands, defensive acquisitions, lawsuits against the raider and mergers -- will be subject to the protection of the business judgment rule.

Panter, Johnson and Treadway, as well as the Second Circuit's decision in Crouse-Hinds Co. v. InterNorth, Inc., 634 F.2d 690 (2d Cir. 1980), make clear that plaintiffs have the burden of rebutting the presumption of the business judgment rule.

In Johnson, the Third Circuit specifically denied a minority shareholder's claim that to rebut the presumption of the business judgment rule, the plaintiff had only to show that perpetuation of control was among the board's motives in making the challenged decisions (which included in this case issuing a control block of stock to one of the directors at a price lower than that offered by plaintiff). Instead, the Court in Johnson held that plaintiff must demonstrate "that impermissible motives predominated in the making of the decision in question" or face a directed verdict based on the business judgment rule.

In Treadway and Crouse-Hinds, the Second Circuit held, respectively, that the mere fact that a challenged action was intended to affect corporate control or that the defendant directors would retain their positions if the defensive action were successful would not, in themselves, constitute a showing of a conflict of interest sufficient to make the business judgment rule inapplicable.

2. Application of the business judgment rule.

a. Bendix-Martin Marietta. -- The extent to which directors have great leeway under the business judgment rule in responding to tender offers was demonstrated in the Martin Marietta-Bendix takeover battle. The Delaware Chancery

Court held that the raider in defending against the counter offer may take steps designed to insure the success of its offer and the defeat of the target's counter offer. Martin Marietta Corp. v. Bendix Corp., Civil Action No. 6942 (Del. Ch. Sept. 19, 1982). The Delaware Chancery Court upheld the call by Bendix of a special meeting of shareholders on the statutory minimum 10-day notice for the purpose of adopting "shark repellants" designed to prevent the removal of the Bendix directors by the written consent of the holder of a majority of the Bendix shares (i.e., Martin Marietta assuming the success of its offer) and to require a super-majority shareholder vote to approve a merger with Martin Marietta. On appeal, the Delaware Supreme Court expressly reserved on the legality of the proposed amendments and the procedure used by the Bendix Board in recommending the amendments to shareholders; the Court found that the Chancery Court had not abused its discretion in refusing to enjoin the Bendix shareholder meeting. Martin Marietta Corp. v. Bendix Corp., No. 298 (Del. Sup. Sept. 21, 1982).

It should be noted that the New York Stock Exchange did not oppose the holding of the Bendix shareholder meeting on such short notice even though the Exchange's normal policy contemplates a 30-day notice period.

In declining to enjoin the Martin Marietta offer even though Bendix had purchased 70% of the Martin Marietta

stock, the Maryland Federal Court cited Martin Marietta's fiduciary duty to its shareholders and the shareholders of Bendix -- not the management of Bendix. The Court also concluded that as the majority shareholder of Martin Marietta, Bendix had a duty to the other Martin Marietta shareholders not to force abandonment of the Martin Marietta offer. Martin Marietta Corp. v. Bendix Corp., No. Y-82-2560 (D. Md. Sept. 22, 1982).

b. American General-NLT. -- The decision in American General Corp. v. NLT Corp., [1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,808 (S.D. Tex. 1982) is another example of the courts' refusing to intervene in a counter-tender offer situation. The Court rejected American General's argument that the counter-tender offer was "manipulative" and refused to find any violations in a welter of charges of incomplete disclosure of future plans. The Court also held that it is not necessary in a first-step partial cash tender offer to give full prospectus-type information with respect to a second-step securities merger.

3. Limits of the business judgment rule.

The business judgment rule will not protect directors who breach fiduciary obligations imposed by other statutes. In Donovan v. Bierwirth, 538 F. Supp. 463 (E.D.N.Y. 1981), aff'd, 680 F.2d 263 (2d Cir. 1982), a case which arose

out of Grumman Corporation's successful defense against a hostile tender offer by LTV Corporation, the Court found that the trustees of Grumman's pension plan, who included members of Grumman's management, breached their fiduciary duties under ERISA in causing the plan to reject the LTV tender offer and to purchase Grumman stock in the face of the tender offer. The Court held that, while ERISA recognizes that fiduciaries may have dual loyalties when acting on behalf of the plan, a trustee's primary loyalty to the plan "is the only loyalty which may affect his judgment." While the opinion should not be read as absolutely prohibiting purchases of target stock by target benefit plans of which target management are the fiduciaries, plan trustees should be certain that appropriate professional advice is sought and that all their decisions are properly documented.

I. Other attacks on target defensive activity.

1. Mobil v. Marathon and "manipulation."

In Mobil Corp. v. Marathon Oil Co., 669 F.2d 366 (6th Cir. 1981) the Court of Appeals for the Sixth Circuit reversed the denial of a preliminary injunction against the unissued stock and "crown jewel" asset options granted to U.S. Steel by Marathon. In the view of the Court of Appeals, the options, both individually and in combination, were intended to choke off a potential auction for control of

Marathon; they accordingly had "the effect of circumventing the natural forces of market demand in this tender offer contest," and thereby constituted "'manipulative acts' in the connection with the tender offer, violative of Section 14(e) of the Williams Act." In the opinion of the Court, this was true even if the Marathon directors acted in "good faith and loyalty" in issuing the options to U.S. Steel in order to enlist U.S. Steel as a white knight: the illegality would then flow from "the conduct of U.S. Steel in demanding and obtaining the option." As relief, the Court directed that the U.S. Steel offer be kept open for a reasonable period of time (without benefit of the options) and that the withdrawal period under the offer be extended for a sufficient period of time "to permit the acceptance of any competing tender offers" made by other potential bidders who may previously have been deterred from coming forward by the options.

Post-Mobil decisions indicate that "lock-ups" and other defensive actions are not necessarily as inherently vulnerable as Mobil was first thought to suggest and that a properly-structured "lock-up" can still work in particular situations. See Buffalo Forge Co. v. Ogden Corp., Civ. 81-29C (W.D.N.Y. January 27, 1983) (after full trial, $26 per share combined stock and option sale to "white knight" in connection with a $32.75 merger agreement held not manipulative within

meaning of Mobil because it was not intended to and did not stifle bidding); Whittaker Corp. v. Edgar, 535 F. Supp. 933 (N.D. Ill. 1982) (agreement to sell the medical division was not a "lock-up" within the Mobil holding inasmuch as it did not create an artificial price ceiling in the tender offer market and was not expressly designed solely for the purpose of completely blocking normal, healthy market activity); Marshall Field & Co. v. Icahn, 537 F. Supp. 413 (S.D.N.Y. 1982) (right of first refusal granted to Batus on Marshall Field's Chicago division for a one-year period following any termination of the two companies' merger agreement found distinguishable from the Yates field option in Marathon; Court states strongly, in dictum, that the Second Circuit would not be likely to follow the Sixth Circuit decision in Marathon). See also Martin Marietta Corp. v. Bendix Corp., No. Y-82-2560 (D. Md. Sept. 22, 1982) (target may legally mount a counter-tender offer defense without violating the antimanipulation provisions of the federal securities laws); American General Corp. v. NLT Corp., [1982 Transfer Binder] Fed. Sec. L. Rep. ¶ 98,808 (S.D. Tex. 1982) (same).