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Share Purchase Rights Plans: An Update and a New Plan

Introduction

We have developed a new share purchase rights plan. Like its predecessors it will undoubtedly be called a "poison pill." This is a most unfortunate misnomer. It is neither a pill nor poisonous. It is merely a compact between a company and its shareholders designed to protect against takeover abuses and assure the shareholders of a fair price and fair treatment.

The new plan provides more protection against takeover abuses than our original plan by deterring unsolicited acquisitions of 20% or more of a company's stock. It also meets concerns about shareholder democracy by providing for a shareholder referendum with respect to fair cash offers for all shares of a company. The new plan is best understood against the background of the takeover abuses it is designed to protect against and the evolution of these plans in practice and in the courts since we developed the first plan almost four years ago. Appendix A contains a summary of the terms of the new plan.

Takeover Abuses

The corporate raider has an extensive arsenal of powerful takeover weapons. The raider can:

- through selective open-market purchases take over a target without the shareholders getting the protections of the federal tender offer rules (the so-called "creeping tender offer");

- "free ride" by acquiring a 5%-20% position and then putting the target "in play" by proposing to acquire the target at more than the average cost of the raider's position, but less than a fair price;

- ignore moral obligations to employees, customers, suppliers and communities and bust up a target to get the last penny of value out of its assets;

- start a tender offer that results in professional speculators acquiring large numbers of shares, then terminate the tender offer and "sweep the street", thereby acquiring control from the speculators, but leaving the small public shareholders as minority shareholders;

- take over a target through a creeping or partial tender offer and then take advantage of the public minority

shareholders through self-dealing and conflict transactions;

- through a partial tender offer take over a target and then squeeze out the public shareholders, forcing them to accept questionable securities;

- commence a takeover raid -- put a target in play -- with no financing commitments whatsoever;

- put a target in play by proposing a takeover price that, while more than current market, is inadequate and unfair to the target's shareholders;

- mobilize institutional shareholders to attack any attempt by a target to defeat a takeover and remain an independent company;

- seek greenmail by threatening one or more of these abusive takeover tactics;

- usurp the traditional functions of a board of directors to act and negotiate on behalf of the shareholders in a merger by making a tender offer that leaves the target with a highly compressed timeframe for considering alternatives and no practical choice other than to find a higher value takeover or pursue a drastic restructuring; and

- take advantage of tax laws that encourage the use of junk bonds and accounting rules that favor acquisitions over research and development and investment in new plant and equipment.

The efficacy of these weapons has been proven on the battlefield. The corporate raider almost always profits. One is hard pressed to name even one major company that in the past five years, without resorting to greenmail, has remained both independent and unrestructured after having become the target of a tender offer. Indeed, very few companies survive merely being put in play by a corporate raider. Corporate raiding has become a major financial activity. The raiders have accumulated billions of dollars of capital through their profitable raids and command tens of billions of dollars of junk bond financing for continuing their raids. While Congress and most state legislatures have and are continuing to study and experiment with legislation to correct takeover abuses, little in the way of meaningful legislation has been enacted and, with the Administration's adamant refusal to recognize the need for takeover reform and the uncertainties as to the constitutional powers of the states in this area, a legislative solution does not seem likely in the immediate future.

Background of the New Plan

From the beginning of the takeover frenzy we have been seeking ways to achieve a fair balance that would not entrench inefficient management but would eliminate the most egregious of the takeover abuses. None has been of sufficient efficacy to be meaningful today other than the rights plan.

The plan has been upheld by most courts that have considered it. (See Appendix B for a summary of the court decisions to date.) Over 450 companies have adopted the plan, including 168 (or 34%) of the Fortune 500 companies and 84 (or 42%) of the Fortune 200 companies. In fact, more Fortune 500 companies have adopted plans than had "fair price" provisions in their charters as of the beginning of 1987. (Appendix C contains a list of the Fortune 500 companies that have adopted plans to date.)

The basic objectives of the plan are to deter abusive takeover tactics by making them unacceptably expensive to the raider and to encourage prospective acquirors to negotiate with the board of directors of the target by making the plan redeemable for a nominal amount prior to a change of effective control through the acquisition of 20% or more of the target's shares. The plan was designed not to interfere, and has not interfered, with the day-to-day

operations of the companies that have adopted it. Prior to its being activated by a change of control, it has no effect on a company's balance sheet or income statement and it is not taxable to the company or the shareholders. Companies have split their stock, issued stock dividends and combined their stock without interference from the plan. The plan has not hindered public offerings of common stock (including associated rights) or SEC clearance of pooling of interests transactions.

The plan was first developed to deal with the then current two-tier, front-end loaded tender offer and related techniques. The "flip-over" provision of the plan stopped the two-tier, the partial and the creeping tender offers that were intended to be followed by a second-step merger. It accomplished this by giving the target's shareholders rights, that would have to be assumed by a raider in a second-step merger, to buy the raider's common stock at half of its market price. The raider was faced with unacceptable dilution unless it either offered a price that was sufficient to attract the tender of substantially all of the shares and the rights, or negotiated a merger at a price acceptable to the target's board of directors so that the rights were redeemed and thereby removed as an impediment to the acquisition.

It was recognized that the flip-over would not prevent a raider, who was prepared to forego a second-step merger and live with minority share ownership, from acquiring control through a partial tender offer or open market purchases. The original plan could have provided this protection, but the unique nature of the plan dictated restraint until it was tested in court. Furthermore, the flip-over provision would still continue for up to ten years to protect the shareholders from an unwanted squeezeout and thereby enable them to realize the long-term value of the company's stock.

The experience of Crown Zellerbach, which in 1984 became the first company to adopt a plan, illustrates both the protections and intentional limitations of the original plan. Although, after a five-month battle in 1985, Sir James Goldsmith acquired a majority of Crown Zellerbach's stock through a creeping tender offer and a street sweep at an average price of $41 per share, Crown Zellerbach was restructured nine months later with Crown Zellerbach retaining some of its assets and James River Corporation acquiring the remaining assets by exchanging the equivalent of approximately $48 in James River common stock for each share of Crown Zellerbach stock. The plan did not prevent Goldsmith from taking over Crown Zellerbach. But it did provide more than five months in which to take protective steps and

increased the board's bargaining power; it did force Goldsmith to drop his tender offer when the Crown Zellerbach board refused to redeem the rights in favor of pursuing a restructuring plan; and when the management restructuring failed, it did protect the minority shareholders from being squeezed out at the price at which Goldsmith acquired control and resulted in their receiving an almost 20% premium over Goldsmith's price.

Similarly, NL Industries, in the course of its battle with Harold Simmons, was able to effect a successful spin-off of its chemicals business even after its rights became nonredeemable due to Simmons' acquisition of over 20% of NL's stock in open-market transactions. The value of NL's stock (i.e., the combined market value of the common stock together with the preferred stock representing the chemicals business) has exceeded the $15-1/4 tender offer price by Simmons every trading day since Simmons acquired a majority of the stock in a street sweep, and on July 22, 1987 closed at $24-3/8. Here, too, although the plan did not prevent a takeover, it resulted in great benefit to the shareholders.

To deal with the problem of shareholders being locked into a minority position and subjected to self-dealing by a raider, we determined it would be appropriate

to add a "flip-in" to the flip-over. The flip-in gives the shareholders of the target, other than the raider which has acquired 20% or more of the target's shares, the right to cause unacceptable dilution to the raider by purchasing shares of the target at a 50% discount in the event the raider engages in self-dealing. The effectiveness of the flip-in, unlike the flip-over, is dependent upon its discriminatory feature, without which the flip-in would not result in dilution to the raider since the raider would be able to buy additional shares on the same basis as the other shareholders.

We subsequently developed the "back-end" plan, which can be used separately or combined with a flip-over plan, to protect against shareholders being faced with the Hobson's choice of accepting an unfair tender offer or being locked-in as minority shareholders. This plan specifies what the target's board deems a fair price for the company and gives the shareholders the right to have the target purchase their shares at that price if the raider does not do so after obtaining control. This back-end plan was used successfully by Phillips Petroleum in defending against Carl Icahn and was sustained by the Supreme Court of Delaware in the Revlon case. However, it has the disadvantage of causing creditors rights problems and there is an issue whether, when triggered, the basic back-end plan is a tender

offer that must comply with the tender offer rules, including the recently adopted all-holders rule that would require that the raider be treated the same as the public shareholders.

In November 1985, the Delaware Supreme Court upheld the basic flip-over plan in the Household case, thereby providing solid legal support for adoption of rights plans and opening the door to further variations of the plan. The Court in Household stated that the adoption of the plan was authorized under Delaware law and governed by the business judgment rule. In response to suggestions that prospective defensive measures are unwarranted, the Court stated, "[t]o the contrary, pre-planning for the contingency of a hostile takeover might reduce the risk that, under the pressure of a takeover bid, management will fail to exercise reasonable judgment. Therefore, in reviewing a pre-planned defensive mechanism it seems even more appropriate to apply the business judgment rule."

The Household decision also established that adoption of a plan does not change the fiduciary standards to be followed by a board of directors in responding to a subsequent takeover bid. As the Court stated, the board "will be held to the same fiduciary standards any other board of directors would be held to in deciding to adopt a defensive

mechanism, the same standard as they were held to in originally approving the Rights Plan." In the event of a specific takeover bid, the plan and its operation will have to be assessed in light of the response that the board decides is appropriate based on the advice of the company's investment banker and legal counsel at that time.

Following the Household decision, many companies adopted plans with flip-in provisions that are not limited to self-dealing but prevent a creeping or partial tender offer because they are triggered at a specific ownership threshold, usually 30%-50%. Under this provision, upon the raider crossing the specified threshold, all the target's other shareholders are given the right to purchase additional shares of the target at half price. Unlike the basic flip-over plan, however, this type of flip-in has had mixed results in the courts, although it does provide greater protection against takeover abuses. Because of our concerns over its legal status, we have in the past recommended adoption of plans without this type of flip-in. We have included it in our new plan, however, because we believe that the special shareholder meeting procedure also included in the new plan will meet any judicial concerns about legality.

The New Plan

The new plan combines the flip-over and flip-in features at a 20% threshold with a provision for a special meeting of shareholders to vote on redemption of the rights where a cash offer for all the target's shares is proposed at a fair price. The flip-in at a 20% threshold will provide greater protection against current takeover abuses while the special meeting procedure provides an avenue for the raider to pursue its takeover that is less subject to abuse. Thus, prior to a raider crossing the 20% threshold, the rights issued under the new plan are redeemable at nominal cost by the directors and, where the offer meets fairness standards, the shareholders can, by a vote of a simple majority of the outstanding shares, override a decision by the directors not to redeem.

To avail itself of the special shareholder meeting a bidder, at the time it requests the meeting, cannot own more than 1% of the target's shares and in the prior twelve months cannot have owned more than 1% at a time when it disclosed or caused the disclosure of an intent to acquire or influence control of the target. This prevents greenmailing and free-riding. The 1% threshold limits the profit potential to a level that makes it unlikely that the bidder is attempting to put the target in play for the pur-

pose of greenmail or to profit from the target being forced to seek a white knight or pursue a drastic restructuring. The twelve-month provision prevents a bidder from evading the 1% threshold by acquiring a 5%-20% position, announcing a takeover proposal, selling down to a 1% position at a profit based on its proposed price and then requesting the special meeting. In addition, to avail itself of the special meeting, the bidder must have financing or financing commitments; furnish an opinion, addressed to the target's shareholders, of a recognized national investment banking firm that the price the bidder is proposing is fair; and agree to bear half of the costs of the special meeting.

In connection with the special shareholder meeting, the bidder may submit any information it wishes for inclusion in the company's proxy statement and may mail its own proxy material if it so desires. The company may include any information of its own it wishes in its proxy material, including information relating to the "fairness" of the price proposed by the bidder and information about any alternative transactions. There would be no restriction on the board of directors determining that the company should remain independent and unrestructured and concurrently with the proxy solicitation for the special shareholder meeting asserting any litigation or other defenses the company wishes. We recognize that obtaining an injunction

against a tender offer is made more difficult by providing for the special shareholder meeting in that some courts will be reluctant to stop a tender offer that the shareholders are about to vote upon; however, we think this risk is a fair trade-off for the protections of the new plan. Nor is there any restriction on the bidder pursuing its takeover effort, including making purchases of up to 20% of the outstanding shares or commencing litigation to invalidate the plan or require the board of directors to redeem the rights, while concurrently pursuing the special meeting.

Prior to the vote at the special shareholder meeting neither the bidder, nor anyone else, could cross the plan's 20% threshold without triggering the nonredeemability and flip-in provisions of the plan at that level.

To assure sufficient time to consider the bidder's proposal and to seek and evaluate alternatives and to prepare the proxy material, but also to avoid undue delay, the special shareholder meeting is required to be held not later than 120 days nor earlier than 90 days after the bidder's request (except that if the bidder's request is received after an annual or special shareholder meeting has been scheduled, the meeting requested by the bidder may be held not later than 120 days after the earlier scheduled meeting). The record date for the meeting would be set in

accordance with applicable law and the company's charter and by-laws. We recognize that the meeting procedure permits the vote to be heavily influenced by arbitraguers (and the bidder and its allies) who purchase shares after the announcement of the bidder's proposal but before the record date for the meeting. However, absent statutory authority, there is a substantial question as to the legality of a record date prior to the first announcement of the bidder's proposal and it would raise other legal questions to restrict purchases by the bidder after it makes its request or to deprive the bidder of voting rights on those purchases.

If a majority of the company's outstanding shares are voted in favor of the resolution at the special shareholder meeting, the rights would be redeemed so as to permit consummation of the bidder's proposal or a competing better proposal. If following an approving vote the company does not enter into a cash merger agreement with the bidder -- and there would be no obligation to do so -- the bidder could make a tender offer unaffected by the plan, provided the tender offer is for all the shares at a cash price not less than the price the shareholders voted upon. The bidder may start its tender offer when it makes the request for the special shareholder meeting or at any time thereafter. If the bidder does so, it can structure the timing so that it

consummates its tender offer immediately following the meeting.

Impact of the New Plan

To the extent that the new plan channels takeover activity into the special shareholder meeting procedure, it will discourage abusive takeover tactics and will provide more time for a target to deal with the cash offer for all shares against which there is today no practical defense other than drastic restructuring. The new plan recognizes the realities of a market dominated by institutional investors and a regulatory system that tolerates junk-bond-financed corporate raiders who are able to put almost any company into play and whose activities invariably result in a bust-up of the target, whether by the raider, a white knight or the target itself in a restructuring.

We recognize that the new plan assures a raider that it can obtain a shareholder vote on a proposed takeover, and, therefore, might be said to promote takeovers. However, as a practical matter, a raider can obtain a shareholder vote, or the pragmatic equivalent of a shareholder vote, on a proposed takeover apart from the special shareholder meeting provisions in the new plan. For most major public companies with substantial institutional ownership there is no absolute takeover defense, other than management

control of a majority of the voting stock. Therefore, those companies and their shareholders are best served by a plan that provides the most effective protection against takeover abuses and removes much of the profit incentive for a raider putting a company in play.

The new plan borrows from the special shareholder meeting concept of the Indiana-type control share acquisition statute recently upheld by the Supreme Court in the CTS case but without its drawbacks. The Indiana-type statute does not protect shareholders from two-tier offers, partial offers, unfair second-step freeze-out mergers, being locked into minority positions or a raider free-riding or seeking greenmail by accumulating up to a 20% position and then putting the target in play. The new plan prevents or protects against all of these abuses, and would reduce the pressure for Delaware and other states to enact the Indiana-type statute.

The Indiana-type statute provides only 50 days to evaluate an offer and to seek and evaluate alternatives, a period that is clearly inadequate for the creation and accomplishment of a complex restructuring or the search for, and negotiation of, an alternative acquisition and the preparation and SEC clearance of the requisite proxy material. The new plan does not affect the bidder's voting rights or

otherwise prevent, any more than the old plan, a tender offer by the bidder from being completed in the 20 business day period set under the Williams Act. Therefore the new plan is not inconsistent with the Williams Act and does not create the sort of preemption question that is thought to limit Indiana-type statutes to the 50-day period. The new plan only establishes a 90 to 120 day period if a bidder desires to avail itself of the special shareholder meeting procedure. If the bidder does not elect to avail itself of this procedure, subject to the other provisions of the plan, it may proceed with a tender offer, open market accumulation or bear hug just as it would at present.

The Debate over Rights Plans

Rights plans have been anathema to the efficient market theorists of the Chicago School whose concept of a free market for corporate control is used as a policy justification by the opponents of plans. The evidence, however, does not support their argument that rights plans hurt shareholder values. Every major investment banking firm that has studied the subject has concluded that adoption of a rights plan has no effect on the stock market prices of companies that were not subject to takeover speculation. An October 23, 1986 study by the SEC's Office of the Chief Economist of stock prices one day before and one day after

adoption of plans did conclude that "poison pills are harmful to target shareholders, on net." After eliminating over 25% of the companies in the survey because of so-called confounding events, such as earnings announcements, dividend increases, Schedule 13D filings or competing takeover bids, the SEC study found a "statistically significant" reduction of stock prices of 0.66%. The SEC's analysis of the entire sample of 245 companies found no statistically significant reduction of stock prices. Focusing specifically on plans that included the so-called "discriminatory flip-in" feature (which is included in our new plan) and eliminating "confounding events," the SEC did find a statistically significant reduction of stock prices both for companies not subject to takeover speculation (a less than 1% reduction) and for companies subject to takeover speculation (a 2.21% reduction). However, none of the flip-in plans studied by the SEC included the provision for a special shareholder meeting as in our new plan.

Contrary to the assertions of its critics, rights plans have not precluded all unsolicited takeovers. Fifty-one companies which had plans have been acquired or are parties to agreements to be acquired, including 42 companies which were acquired after receiving unsolicited bids or having a substantial percentage of its stock acquired by a

party seeking control (18 of which adopted plans after receiving such bids).

The evidence suggests, however, that the plan has indeed served its intended purpose of increasing the bargaining power of the target's board of directors -- even in situations where the target is acquired by the initial bidder. Acquirors launching hostile bids against companies with plans in all cases initially condition their bids on the rights being redeemed or nullified. Furthermore, as shown in Appendix D, in 33 of the 36 acquisitions that were initiated by unsolicited bids, the price ultimately received by shareholders was higher than the initial bid, including 13 cases in which the premium over the initial bid exceeded $100 million. The aggregate premium paid to shareholders over the initial bids in these 36 cases was $4.7 billion. Thus, the plan clearly serves its principal objectives -- protection against abusive tactics and increased bargaining power resulting in higher prices for shareholders.

Institutional Investors

Several institutional investors have joined the corporate raiders and the SEC to attempt to eliminate the original form of rights plan as a defense against takeover abuses. Earlier this year, the College Retirement Equities Fund (CREF) and the California Public Employees Retirement

System submitted resolutions to some 30 companies, generally those with institutions holding a majority of the outstanding shares, requesting rescission of their plans unless submitted to a shareholder vote and approved by a majority of the shares. These proposals received the support of an average of only about 20% of the outstanding shares and failed to attract a majority of the shares voting at any company that considered them. We believe the provision for a shareholder meeting to request acceptance of an offer addresses many of the shareholder democracy concerns raised by the institutions supporting these proposals.

Conclusion

The takeover frenzy continues and the dynamics of takeovers are constantly changing. At the same time many institutional investors deem protection against takeover abuses to be an infringement on their rights as shareholders. In addition, there is an adverse reaction in Congress and some state legislatures to takeover defenses that may infringe on shareholder democracy. The new plan we have developed is designed to cope with the new takeover tactics while at the same time dealing with the concerns over shareholder democracy and allaying any fears of directors that, even though fulfilling their fiduciary duties by rejecting what they believe to be an inadequate offer, they may not be

doing what the shareholders desire. We recommend that those companies that do not have a plan consider adopting the new plan and those that have a plan consider substituting the new plan for the original plan.

While we believe that the new plan, if universally adopted, would decrease hostile takover activity, it will not, and is not intended to, make a company takeover-proof. Like its predecessor it protects against the worst takeover abuses, it gives all parties a reasonable period of time in which to make decisions on such a fundamentally important question as a takeover, and it strengthens the ability of the board of directors of a target to fulfill its fiduciary duties to obtain the best result for the shareholders.

As in the case of the original plan, and most significant legal innovations, there can be no assurance that all courts will agree that the new plan is legal. It is our opinion that it is legal and that it is within the business judgment of the board of directors to substitute the new plan for the original plan.

Martin Lipton
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APPENDIX A

Terms of New Plan Rights*

Issuance: One right to buy one one-hundredth of a share of a new series of preferred stock as a dividend on each outstanding share of common stock of the company. Until the rights become exercisable, all further issuances of common stock, including common stock issuable upon exercise of outstanding options, would carry the rights.

Term: 10 years.

Exercise price: An amount per one one-hundredth of a share of the preferred stock which approximates the board's view of the long-term value of the company's common stock. Most companies that have adopted rights plans have fixed the exercise price at between three and four times current market price. Factors to be considered in setting the exercise price include the company's business and prospects, its long-term plans and market conditions. The exercise price is subject to certain anti-dilution adjustments. For illustration only, assume an exercise price of $150 per one one-hundredth of a share.

Rights detach and become exercisable: Prior to such time as a person or group acquires beneficial ownership of 20% or more of the company's common stock or announces its intention to commence a tender or exchange offer the consummation of which would result in beneficial ownership by such person or group of 30% or more of the company's common stock, the rights are not exercisable and are not transferable apart from the company's common stock. As soon as practicable after the rights become exercisable, separate rights certificates would be issued and the rights would become transferable apart from the company's common stock.

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* These terms are as they would be set by a company that does not have sufficient authorized shares of common stock to enable the rights to be exercisable for common stock and, in lieu of common stock, uses authorized blank check preferred stock, with terms that make 1/100th of a share of the preferred stock the ecomomic equivalent of one share of common stock, as the security for which the rights are exercisable.

Protection against squeezeout: If, after the rights have been triggered, an acquiring company were to merge or otherwise combine with the company, or the company were to sell 50% or more of its assets or earning power, each right then outstanding would "flip over" and thereby would become a right to buy that number of shares of common stock of the acquiring company which at the time of such transaction would have a market value of two times the exercise price of the right. Thus, if the acquiring company's common stock at the time of such transaction were trading at $75 per share and the exercise price of the rights at such time were $150, each right would thereafter be exercisable at $150 for four shares (i.e., the number of shares that could be purchased for $300, or two times the exercise price of the right) of the acquiring company's common stock.

Protection against creeping acquisition/open market purchases: In the event a person or group were to acquire a 20% or greater position in the company, each right then outstanding would "flip in" and become a right to buy that number of shares of common stock of the company which at the time of such acquisition would have a market value of two times the exercise price of the right. The acquirer who triggered the rights would be excluded from the "flip-in". Thus, if the company's common stock at the time of the "flip-in" were trading at $75 per share and the exercise price of the rights at such time were $150, each right would thereafter be exercisable at $150 for four shares of the company's common stock, again providing a dilutive 50% discount.

Redemption: (a) The rights are redeemable by the company's board of directors at a price of $.02 per right at any time prior to the acquisition by a person or group of beneficial ownership of 20% or more of the company's common stock. Thus, the rights would not interfere with a negotiated merger or a white knight transaction, even after a hostile tender offer has been commenced or the special meeting described below has been scheduled or held. The rights may prevent a white knight transaction after a 20% acquisition.

(b) The rights would be automatically redeemed for $.02 per right if a tender offer is consummated during the 60-day period following a special meeting at which shareholders request the board to accept an acquisition proposal, provided that the tender offer is at a price per share in cash at least as high as the price offered in such proposal and no person or group has yet acquired beneficial ownership of 20% or more of the company's common stock. The special shareholder meeting would be called within 90 to 120 days of a request by a bidder who has made a proposal to acquire all

of the company's shares for cash at a price which is fair to the company's shareholders in the opinion of a national investment bank retained by the bidder. The bidder could not own more than 1% of the target's shares at the time it requests the special meeting or within the prior year at a time when it disclosed an intent to acquire or influence control of the company. The bidder would also be required to have financing or financing commitments at the time it requests a special meeting and agree to bear half of the costs of the meeting.

Voting: The rights would not have any voting rights.

Terms of preferred stock: The new preferred stock issuable upon exercise of the rights would be non-redeemable and would rank junior to all other series of the company's preferred stock. The dividend, liquidation and voting rights, and the non-redemption feature, of the preferred stock are designed so that the value of the one-hundredth interest in a share of new preferred stock purchasable with each right will approximate the value of one share of common stock. Each whole share of new preferred stock would be entitled to receive a quarterly preferential dividend of $1 per share but would be entitled to receive, in the aggregate, a dividend of 100 times the dividend declared on the common stock. In the event of liquidation, the holders of the new preferred stock would be entitled to receive a preferential liquidation payment of $100 per share but would be entitled to receive, in the aggregate, a liquidation payment equal to 100 times the payment made per share of common stock. Each share of new preferred stock would have 100 votes, voting together with the common stock. Finally, in the event of any merger, consolidation or other transaction in which shares of common stock are exchanged for or changed into other stock or securities, cash and/or other property, each share of new preferred stock would be entitled to receive 100 times the amount received per share of common stock. The foregoing rights are protected against dilution in the event additional shares of common or new preferred stock are issued. Since the "out of the money" rights would not be exercised immediately, registration of the new preferred stock issuable upon exercise of the rights with the Securities and Exchange Commission need not be effective until the rights become exercisable.

Federal income tax consequences: The distribution of the rights is not a taxable event for the company or its shareholders under the federal income tax laws. Nor does the physical distribution of rights certificates upon the rights becoming exercisable result in any tax. After such physical

distribution, the rights would be treated for tax purposes as capital assets in the hands of most shareholders and each right would probably have a basis of zero and a holding period which relates back to the holding period of the stock with respect to which such right was issued. Upon the rights becoming rights to purchase an acquirer's common stock, holders of rights probably would be taxed even if the rights were not exercised. Upon the rights becoming rights to purchase additional common stock of the company, holders of rights probably would not have a taxable event. The rights may have an impact on tax-free reorganizations involving the company. Several types of tax-free transactions can be structured although the rights may be treated as taxable "boot."

Accounting consequences: The initial issuance of the rights has no accounting or financial reporting impact. Since the rights would be "out of the money" when issued, they would not dilute earnings per share. Because the redemption date of the rights is neither fixed nor determinable, the accounting guidelines do not require the redemption amount to be accounted for as a long-term obligation of the company. The rights do raise certain issues with respect to pooling of interests transactions, but several Big-Eight accounting firms have advised that the rights should not interfere with a company's ability to consummate a pooling transaction so long as the transaction is properly structured.

Miscellaneous: The Rights Agreement provides that the company may not enter into any transaction of the sort enumerated in the squeezeout provision if in connection therewith there are outstanding securities or there are agreements or arrangements intended to counteract the protective provisions of the rights. The Rights Agreement may be amended from time to time in any manner consistent with the board's purposes in adopting the rights plan, prior to the acquisition by a person or group of beneficial ownership of 20% or more of the company's common stock.

	EXERCISABLE	REDEEMABLE	"FLIP OVER"	"FLIP IN"
TIME	After beneficial ownership of 20% or more of common stock is acquired or After commencement or announcement of tender or exchange offer the consummation of which would result in beneficial ownership of 30% or more of common stock	At any time until beneficial ownership of 20% or more of common stock is acquired, either (a) at the option of the board of directors or (b) automatically in connection with a tender offer at a cash price per share approved by shareholders at a special meeting	Upon merger, other business combination, or sale of 50% or more of assets or earning power	Upon acquisition of beneficial ownership of 20% or more of common stock
PRICE	$150 (for illustrative purposes only) for each 1/100 of a share of new preferred stock	$.02 per Right	After merger, other business combination or sale of 50% or more of assets or earning power, all holders of Rights may purchase $300 market value of acquirer's stock for each Right exercised at $150	After acquisition of beneficial ownership of 20% or more of common stock, all holders of Rights other than the 20% or greater holder may purchase $300 market value of the company's common stock for each Right exercised at $150

Timetable

DATE OR EVENT	SIGNIFICANCE
Declaration Date	Board declares dividend of one right for each share of common stock Each right entitles holder to purchase 1/100 of a share of new preferred stock only upon conditions described below at price of $150 (for illustrative purposes only) Until Distribution Date, rights "trade with" the common stock (i.e., not independently transferable) Rights expire ten years after date of issuance
suance (and Record) Date t least 10 days after Declaration Date)	Effective Date of dividend distribution -- Rights are issued to all holders of common stock on this date, but no Right Certificates will be issued Rights are still not separately transferable because still "trading with" the common stock; Rights still not exercisable
"Distribution Date": Ten days after public announcement of	
(a) Acquisition of 20% or greater "beneficial ownership" by a person or group, or (b) Tender or exchange offer which, if consummated, would result in acquisition by a person or group of 30% or greater "beneficial ownership"	The company mails out Rights Certificates to holders of its common stock as of the Distribution Date Rights become exercisable -- rights can be exercised at rate of one right = 1/100 of a share of new preferred stock; Exercise Price = $150 (for illustrative purposes only) per 1/100 of a share, subject to certain anti-dilution adjustments Rights become transferable

Timetable - continued

DATE OR EVENT	SIGNIFICANCE
Acquisition of 20% or greater "beneficial ownership" by a person or group	Rights "flip in" Rights can be exercised (except by person or group beneficially owning 20% or more of the company's common stock) to acquire common stock of the company with a market value of two times the exercise price (i.e., $300 worth of common stock), unless adjusted
Acquisition of the company in merger or Transfer of 50% or more of ~e company's assets or ~rning power	Rights "flip over" Rights can be exercised to acquire common stock of acquiring company with a market value of two times the exercise price (i.e., $300 worth of common stock), unless adjusted
Redemption	Prior to the acquisition by a person or group of "beneficial ownership" of 20% or more of the company's common stock, rights are redeemable for $.02 per share either (a) at the option of the board or (b) automatically in connection with consummation of a tender offer at a cash price per share approved by shareholders at a special meeting Note: Announcement of a tender or exchange offer the consummation of which would result in beneficial ownership by a person or group of 30% or more of the common stock does not terminate the redemption right

Court Decisions on Rights Plans

The Household case was the beginning of the litigation attacks on the rights plan, not the end. There has been a mixed bag of decisions with a few lower courts, applying the laws of states other than Delaware, accepting arguments that were rejected by the Supreme Court of Delaware. On balance, however, it appears that most courts will follow the Household decision and today there is relatively little doubt as to legality of the basic flip-over plan. Furthermore, the Gelco, CTS II and Harvard Industries decisions illustrate that the validity of plans containing discriminatory "flip-in" features is widely recognized by the courts.

The court decisions on plans are distinguished below based upon whether they upheld the particular plan in question:

A. Upheld Rights Plans

1. Moran v. Household International, Inc., 500 A.2d 1346 (Del.), aff'g 490 A.2d 1059 (Del. Ch. 1985) (flip-over plan)

2. Horwitz v. Southwest Forest Industries, Inc., 604 F. Supp. 1130 (D. Nev. 1985) (flip-over plan; Court denied injunction relying on Delaware Chancery Court decision in Household)

3. APL Corp. v. Johnson Controls, Inc., 85 Civ. 990 (E.D.N.Y. March 25, 1985) (flip-in plan applying Wisconsin law; Court denied injunction relying on Delaware Chancery Court decision in Household)

4. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986), aff'g 501 A.2d 1239 (Del. Ch. 1985) (back-end plan)

5. Edelman v. Phillips Petroleum Co., C.A. No. 7899 (Del. Ch. June 3, 1986) (flip-in plan instituted in connection with settlement of class action litigation)

6. Dynamics Corp. of America v. CTS Corp., 635 F. Supp. 1174 (N.D. Ill.), aff'd in part and vacated in part, 805 F.2d 705 (7th Cir. 1986) ("CTS II") (back-end plan applying Indiana and Delaware law; District Court refused to

enjoin plan; Seventh Circuit remanded for further consideration as to whether the procedure by which the rights plan had been formulated and recommended for adoption met the requisite standards of reasonableness and good faith, but held that the basic concept of the rights plan is valid and legal under Indiana and Delaware law and that the discrimination against certain large shareholders is discrimination among shareholders, not among shares, and, therefore, is not in violation of the statutory prohibition against discrimination among shares)

7. Allied Stores Corporation v. Campeau Acquisition Corp., 86 Civ. 7841 (PNL) (S.D.N.Y. Oct. 24, 1986) (back-end plan applying Delaware law; Court refused to grant TRO)

8. N.V. Homes v. Ryan Homes, Civ. No. 86-2139 (W.D. Pa. Oct. 24, 1986) (back-end plan; Court refused to preliminarily enjoin plan)

9. Gelco Corp. v. Coniston Partners, 652 F. Supp. 829 (D. Minn. 1986), aff'd in part and vacated in part, 811 F.2d 414 (8th Cir. 1987) (flip-in plan; Court specifically rejected the NL decision and held that adoption of a rights plan was not ultra vires)

10. Harvard Industries, Inc. v. Tyson, [Current] Fed. Sec. L. Rep. (CCH) ¶ 93,064 (E.D. Mich. Nov. 25, 1986) (flip-in plan; Court denied request for preliminary injunction, holding that discrimination was among shareholders and was not therefore prohibited)

11. Spinner Corp. v. Princeville Development Corp., [Current] Fed. Sec. L. Rep. (CCH) ¶ 93,058 (D. Haw. 1986), vacated [Current] Fed. Sec. L. Rep. (CCH) ¶ 93,157 (D. Haw. 1987) ("Spinner") (flip-over provisions of rights plan applying Colorado law; Court refused to enjoin such provisions on the grounds that they did not discriminate among shareholders; see below)

B. Invalidated Rights Plans

1. Dynamics Corporation of America v. CTS Corporation, 637 F. Supp. 406 (N.D. Ill.), aff'd, 794 F.2d 250 (7th Cir. 1986), rev'd on other grounds, 95 L. Ed. 2d 67, 107 S. Ct. 1637 (1987) ("CTS I") (flip-in plan applying Indiana and Delaware laws; Court enjoined plan on basis that the CTS directors had not satisfied the requirements of the

business judgment rule, and questioned the validity of the flip-in provisions on the basis of mere ownership of 15% of the common stock)

2. Amalgamated Sugar Co. v. NL Industries, Inc., 644 F. Supp. 1229 (S.D.N.Y. 1986) (flip-in plan applying New Jersey law; Court held that "self-dealing" flip-in provision discriminated against large shareholders in violation of New Jersey law)

3. R.D. Smith & Co., Inc. v. Preway Inc., 644 F. Supp. 868 (W.D. Wisc. 1986) (flip-in plan; Court denied injunction for failure to show irreparable harm, but, in dicta, said that plaintiffs have a good chance of succeeding on the merits, citing NL)

4. Spinner (flip-in and back-end plans applying Colorado law; Court enjoined "self-dealing" flip-in provisions because of discriminatory features but left intact flip-over provisions; see above)

5. Buckhorn Inc. v. Ropak Corporation, 656 F. Supp. 209 (S.D. Ohio), aff'd by sum. ord., 815 F.2d 76 (6th Cir. 1987) (back-end plan applying Delaware law; while adoption of the back-end plan was a "reasonable response to the threat perceived," the particular plan was invalidated due to the board's failure to exercise due care in setting the exercise price for the plan, citing several flaws in the financial analysis presented to the board)

C. Other Issues

1. Holstein v. UAL Corporation, No. 87 C 3888 (N.D. Ill. June 9, 1987) (rights plan not actionable as a tender offer under the Williams Act at least until the rights become exercisable)

Fortune 500 Companies With Plans

Company	Sales Rank	Company	Sales Rank
Mobil	5	Dresser Industries	105
Texaco	8	Owens-Corning Fiberglas	107
United Technologies	17	Owens-Illinois	108
Occidental Petroleum	19	Borg-Warner	110
Atlantic Richfield	20	Scott Paper	115
Allied-Signal	25	Cooper Industries	116
Goodyear Tire & Rubber	29	Control Data	119
Lockheed	30	Mead	125
Phillips Petroleum	31	GenCorp	128
Xerox	32	Armco	129
Kraft	37	Diamond Shamrock	130
Anheuser-Busch	43	FMC	131
Unisys	46	Staley Continental	132
Caterpillar	47	Avon Products	135
Raytheon	48	Gillette	137
Honeywell	52	Burlington Industries	140
Ashland Oil	54	Johnson Controls	147
Monsanto	55	Hercules	148
W.R. Grace	56	B.F. Goodrich	150
TRW	58	Kerr-McGee	152
ConAgra	59	Squibb	153
Pillsbury	61	INTERCO	154
Weyerhaeuser	62	Lear Siegler	156
Ralston Purina	65	Schering-Plough	157
International Paper	66	Cummins Engine	160
American Brands	68	Upjohn	162
Textron	69	R.R. Donnelley & Sons	164
Borden	70	Harris	166
Colgate-Palmolive	71	Emhart	170
NCR	75	National Distillers & Chemical	171
Martin Marietta	77	Union Camp	173
Aluminum Co. of America	79	Great Northern Nekoosa	174
General Mills	80	Tribune	176
CPC International	81	Pitney Bowes	178
Champion International	86	Morton Thiokol	184
American Cyanamid	94	Allegheny International	186
Eaton	95	Armstrong World Industries	187
Time Inc.	98	Knight-Ridder	189
Boise Cascade	100	Zenith Electronics	191
Firestone Tire & Rubber	102	Valero Energy	192
Dana	103	Corning Glass Works	193
Quaker Oats	104	Maytag	194

Company	Sales Rank	Company	Sales Rank
Parker Hannifin	201	Bell & Howell	338
Brunswick	202	Rorer Group	341
Olin	204	Louisiana Land & Exploration	348
Int'l. Minerals & Chemical	205	Economics Laboratory	352
Koppers	206	Cyprus Minerals	354
J.P. Stevens	208	Hughes Tool	355
Polaroid	211	Rubbermaid	360
General Signal	214	Tandem Computers	364
McGraw-Hill	217	Reichhold Chemicals	366
Mapco	218	Anchor Hocking	367
Baker International	220	Mohasco	368
Stanley Works	221	Insilco	374
TRINOVA	231	Nalco Chemical	375
Sundstrand	236	Interlake	376
Square D	238	Ferro	377
International Multifoods	240	Nashua	381
Becton Dickinson	248	Dennison Manufacturing	382
Cabot	249	Joy Manufacturing	388
NL Industries	252	AM International	390
Data General	255	Sealed Power	392
Crane	264	Southwest Forest Industries	394
Willamette Industries	265	Dexter	396
G. Heileman Brewing	267	Eagle-Picher Industries	397
EG&G	270	Texas Industries	398
Avery International	273	Warnaco	405
Norton	277	Rohr Industries	407
Rexnord	281	Pentair	411
Ball	285	Kellwood	438
Hartmarx	288	C.R. Bard	448
Mattel	289	H.B. Fuller	457
Timken	290	Dorsey	458
Arvin Industries	298	Carpenter Technology	461
Outboard Marine	306	Phillips-Van Heusen	462
Gerber Products	308	Hon Industries	466
Nortek	313	Kenner Parker Toys	467
Chicago Pacific	317	Coleman	468
Clark Equipment	318	Computervision	471
Federal-Mogul	320	Tambrands	476
Bowater	324	Scientific-Atlanta	478
Varian Associates	325	Moore McCormack Resources	480
Dayco	326	Clevite Industries	484
M/A-Com	331	Barnes Group	486

APPENDIX D

Companies Acquired After Adoption of Rights Plans

As of July 22, 1987, at least 51 companies with rights plans -- over 10% of all companies which have adopted rights plans -- have been acquired (or are parties to definitive agreements to be acquired). These include 24 companies which had adopted rights plans prior to the receipt of unsolicited bids or substantial stock accumulation by a party seeking control (13 of which were acquired by white knights), 18 companies which adopted rights plans after unsolicited bids had been made (10 of which were acquired by white knights), and 9 companies which were acquired following initial friendly agreements (2 of which were acquired by subsequent unsolicited bidders). With the exception of Allied Stores, Crown Zellerbach, NL Industries, Revlon and William E. Wright, all of the acquisitions of control by unsolicited bidders followed negotiated agreements.

A. Plans Adopted Before Bid

1. Companies Acquired by Unsolicited Bidder

Anchor Hocking
Crown Zellerbach
Day International
Ex-Cell-O
Hayes-Albion
Healthcare USA
NL Industries
Ponderosa
Research-Cottrell
Rexnord (19% holder had challenged restructuring plan)
Ryan Homes

2. Companies Acquired by White Knight After Unsolicited Bid

Borg-Warner
Burlington Industries
Clevite (hostile bid had topped management LBO)
Harper & Row
Joy Manufacturing
Lear-Siegler
Morse Shoe
Planning Research
Raymond Engineering (25% holder warned of proxy fight)
Safeway Stores
Southland
Supermarkets General
TRE Corp. (17% holder had commenced proxy fight)

3. Companies Acquired by Unsolicited Bidder Following Friendly Agreement

Purolator Courier
Viacom

4. Companies Acquired Without Unsolicited Bid

Eastern Air Lines
Hughes Tool
McNeil Corp.
Owens-Illinois
RCA
Southwest Forest Industries

B. Plans Adopted After Bid

1. Companies Acquired by Unsolicited Bidder

Allied Stores (Back-end plan)
Associated Dry Goods
Great Lakes International (Back-end plan)
Revlon (Back-end plan)
Trico (21% holder had stated it might seek control)
Victory Markets
Warnaco (Bid followed friendly agreement)
William E. Wright

2. Companies Acquired by White Knight After Unsolicited Bid

AMSTED Industries
Baird
Bank Building & Equipment
Chemlawn
Cluett Peabody
Conna
Mayflower Group (Value assurance plan)
Princeville Development
Sea-Land
Westchester Financial Services

3. Companies Acquired Without Unsolicited Bid

Anderson Greenwood

Maximization of Shareholder Values

Six of the acquisitions of companies with plans (AMSTED, Baird, Raymond Engineering, Rexnord, Trico and TRE) were preceded by substantial stock accumulations by parties

which threatened to seek control but which did not make a bid prior to the company entering into a merger agreement. In thirty-three of the thirty-six acquisitions that were initiated by a hostile bid, the price ultimately received by shareholders was higher than the initial bid, including 13 cases where the premium over the initial bid exceeded $100 million. The aggregate premium paid to shareholders over the initial bids in these thirty-six cases was $4.7 billion.

Company	Initial Bid Per Share	Final Price Per Share	% Change	Aggregate $ Increase
Pre-Bid Plan/ Acquired by Unsolicited Bidder				
Anchor Hocking	$34	$32	(6%)	($21 million)
Crown Zellerbach	$42.50	$44.50	5%	$69 million
Day International	$45	$48	7%	$21 million
Ex-Cell-O	$68	$77.50	14%	$128 million
Hayes-Albion	$12.50	$13	4%	$2 million
Healthcare USA	$11	$13.50	23%	$11 million
NL Industries	$15	$23.97*	60%	$302 million
Ponderosa	$27.50	$29.25	6%	$17 million
Research-Cottrell	$35	$43	23%	$52 million
Ryan Homes	$45	$48	7%	$22 million
Subtotal (10 cases)			14%	$603 million
Pre-Bid Plan/ White Knight				
Borg-Warner	$43	$48.50	13%	$476 million
Burlington Indus.	$60	$78	30%	$491 million
Clevite	$11.50	$17.50	52%	$40 million
Harper & Row	$34	$65	91%	$136 million
Joy Manufacturing	$31	$35	13%	$71 million
Lear-Siegler	$85	$92	8%	$125 million
Morse Shoe	$40	$47	18%	$39 million
Planning Research	$28	$31.50	11%	$23 million
Safeway Stores	$58	$69	19%	$335 million
Southland	$65	$77	18%	$586 million
Supermarkets Gen.	$41.75	$46.75	12%	$164 million
Subtotal (11 cases)			26%	$2.5 billion
Total Pre-Bid (21 cases)			21%	$3.1 billion

* Blended price of tender offer purchases and 7/16/87 market price.

Company	Initial Bid Per Share	Final Price Per Share	% Change	Aggregate $ Increase
Post-Bid Plan/ Acquired by Unsolicited Bidder				
Allied Stores	$58	$67.91*	17%	$468 million
Assoc. Dry Goods	.75 shares	.86 shares	15%	$335 million
Great Lakes Int'l	$60	$62.50	4%	$5 million
Revlon	$45	$58	29%	$488 million
Victory Markets	$20	$24.67	23%	$13 million
Warnaco	$36	$46.50	29%	$106 million
William E. Wright	$15.125	$14.54*	(4%)	($1 million)
Subtotal (7 cases)			16%	$1.4 billion
Post-Bid Plan/ White Knight				
Bank Building & Equipment	$14.25	$14	(2%)	($.4 million)
Chemlawn	$27	$36.50	35%	$97 million
Cluett Peabody	$40	$41	3%	$8 million
Conna	$18	$20	11%	$2 million
Mayflower	$29.25	$31.50	8%	$17 million
Princeville Development	$12	$13	8%	$8 million
Sea-Land	$25	$28	12%	$42 million
Westchester Fin.	$30	$53	77%	$45 million
Subtotal (8 cases)			27%	$219 million
Total Post-Bid (15 cases)			18%	$1.6 billion
Grand Total (36 cases)			19%	$4.7 billion

Companies Remaining Independent

Most of the major companies which remained independent despite hostile bids in the last twelve months had plans, including Diamond Shamrock, Gencorp, Goodyear, Gillette, Owens-Corning Fiberglas, Lucky Stores, Gelco and CPC International. All of such companies paid greenmail, restructured or did both.

* Blended front-end and back-end price