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To Our Clients:

Is This The End of Takeovers

The state takeover laws did not stop them. Litigation -- antitrust and other -- did not stop them. The reaction to the PacMan defense of Martin-Marietta against Bendix did not stop them. Shark repellants and poison pills did not stop them. The October 19, 1987 crash did not stop them. And jawboning by the Fed and the failure of the Federated Department Stores junk bond offering will not stop them.

Our Nation is blindly rushing to the precipice. As with tulip bulbs, South Sea bubbles, pyramid investment trusts, Florida land, REITs, LDC loans, Texas banks and all the other financial market frenzies of the past, the denouement will be a crash. We and our children will pay a gigantic price for allowing abusive takeover tactics and boot-strap, junk-bond takeovers. We are overleveraging American companies and forcing them to focus on short-term stock market results. Research, new product development and capital investment are no longer the keys to business success. To the contrary they have become the invitation to a junk-bond, bust-up party. While the rest of the industralized world is investing for the future, we are squandering our assets in a speculative binge of junk bonds, financial futures, program trading, put and call options and the other games of today's financial market casinos.

The only remedy is effective legislation. Perhaps it is already too late. The institutional investors -- who have gained control of virtually every major company -- show no restraint and no regard for the public good. They must be policed. They cannot be allowed to force American business to be denuded of equity and operate with unsustainable levels of debt. We must mandate that they be long-term investors not short-term speculators and promoters of takeovers. American business must get behind a tax on institutional investors which takes away all profit on stock held less than one year and most of the profit on stock held less than five years. In addition, public institutions, like banks, insurance companies, pension funds and mutual funds should be prohibited from loading up on junk bonds.

Curbing the abuses being perpetrated by institutional investors is not enough. As long as our tax laws favor junk bonds over equity, the pressure to overleverage will remain. We must remove the tax advantage that junk bonds enjoy.

At the moment, the courts are our only hope. The poison pill is an effective defense against abusive takeovers. The courts are now recognizing this. Hopefully, they will make it clear that a board of directors does not have to redeem a pill and either auction the company to the highest bidder or restructure by turning equity into debt. In other words, the courts should affirm that a board of directors, acting in good faith and on reasonable grounds, has the absolute right to reject any takeover bid. At other moments in our history, the courts have stepped in to solve social and economic problems that were beyond the Congress. What is necessary today is that they defer to the honest business judgment of boards of directors. While corporate raiders in league with institutional investors may shift from tender offers to proxy fights to force boards into auctions or restructuring, that shift will slow down the process, expose the role of the institutions and further the opportunity for legislation regulating the institutions.

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