

NOTICE OF MEETING

TO: Corporation Law Section Membership

FROM: David B. Brown  
Secretary of the Corporation Law Section

RE: Proposed Section 203-Section  
Meeting of January 4, 1988

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A meeting of the Corporation Law Section will be held at 10:00 a.m. on Monday, January 4, 1988, at the offices of the Corporation Trust Company, 1209 Orange Street to consider the enclosed draft of a proposed Section 203 to the Delaware General Corporation Law.

The Council of the Section and the Subcommittee charged with drafting Section 203 met on several occasions to review various amendments to the draft of Section 203 considered at the last Section meeting on December 11, 1987, as well as others raised in the comment letters received by the Council. The enclosed draft represents a further compromise over the contents of such a statute. The Council of the Corporation Law Section has approved this version of Section 203 by a 14 to 1 vote.

While numerous technical changes have been made to proposed Section 203, the principal amendments to the November 19, 1987 draft previously circulated to the Section are: (1) the statute is now triggered by the acquisition of 15% (up from 10%) of the outstanding voting stock, (2) the percentage of voting stock that must be acquired in the transaction which takes a stockholder over the 15% level in order to avoid the statute's three year moratorium has been decreased to 85% (down from 90%) of the voting stock, with the further condition that stock held by directors who are also officers and by certain employee stock plans are excluded in determining whether the 85% level has been reached, (3) the approval of disinterested stockholders that is required to approve a business transaction during the three year period has been modified to only require a vote of 66.6% of such outstanding voting stock, and (4) an amendment to the bylaws by the stockholders that elects to exclude the corporation from the coverage of Section 203 will become effective 12 months after the amendment is adopted (instead of 18 months as previously proposed), and the time the board of directors may elect to exclude the corporation from the coverage of Section 203 is 90 days (instead of 45 days as previously proposed).

December 23, 1987

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Add a new Section 203 to read as follows:

§ 203      Business Combinations With Interested Stockholders

(a) Notwithstanding any other provision of this chapter, a corporation shall not engage in any business combination with any interested stockholder for a period of 3 years following the date that such stockholder became an interested stockholder, unless (1) prior to such date the board of directors of the corporation approved either the business combination or the transaction which resulted in the stockholder becoming an interested stockholder, or (2) upon consummation of the transaction which resulted in the stockholder becoming an interested stockholder, the interested stockholder owned at least 85% of the voting stock of the corporation outstanding at the time the transaction commenced, excluding for purposes of determining the number of shares outstanding those shares owned (i) by persons who are directors and also officers and (ii) employee stock plans in which employee participants do not have the right to determine confidentially whether shares held subject to the plan will be tendered in a tender or exchange offer, or (3) on or subsequent to such date the business combination is approved by the board of directors and authorized at an annual or special meeting of stockholders, and not by written consent, by the affirmative vote of at least 66-2/3% of the outstanding voting stock which is not owned by the interested stockholder.

(b) The restrictions contained in this section shall not apply if:

(1) the corporation's original certificate of incorporation contains a provision expressly electing not to be governed by this section;

(2) the corporation, by action of its board of directors, adopts an amendment to its bylaws within 90 days of the effective date of this section expressly electing not to be governed by this section, which amendment shall not be further amended by the board of directors;

(3) the corporation, by action of its stockholders, adopts an amendment to its certificate of incorporation or bylaws expressly electing not to be governed by this section, provided that, in addition to any other vote required by law, such amendment to the certificate of incorporation or bylaws must be approved by the affirmative vote of a majority of the shares entitled to vote. An amendment adopted pursuant to this paragraph shall not be effective until 12 months after the adoption of such amendment and shall not apply to any business combination between such corporation and any person who became an interested stockholder of such corporation on or prior to such adoption. A bylaw amendment adopted pursuant to this paragraph shall not be further amended by the board of directors;

(4) the corporation does not have a class of voting stock that is (i) listed on a national securities

exchange, (ii) authorized for quotation on an inter dealer quotation system of a registered national securities association or (iii) held of record by more than 2,000 stockholders, unless any of the foregoing results from action taken, directly or indirectly, by an interested stockholder or from a transaction in which a person becomes an interested stockholder;

(5) a stockholder becomes an interested stockholder inadvertently and (i) as soon as practicable divests sufficient shares so that the stockholder ceases to be an interested stockholder and (ii) would not, at any time within the 3-year period immediately prior to a business combination between the corporation and such stockholder, have been an interested stockholder but for the inadvertent acquisition; or

(6) the business combination is proposed prior to the consummation or abandonment of and subsequent to the earlier of the public announcement or the notice required hereunder of a proposed transaction which (i) constitutes one of the transactions described in the second sentence of this paragraph; (ii) is with or by a person who either was not an interested stockholder during the previous 3 years or who became an interested stockholder with the approval of the corporation's board of directors; and (iii) is approved or not opposed by a majority of the members of the board of directors then in office (but not less than 1) who were directors prior to any person becoming an interested stockholder during the previous 3 years or were recommended for election or elected to succeed such



directors by a majority of such directors. The proposed transactions referred to in the preceding sentence are limited to (x) a merger or consolidation of the corporation (except for a merger in respect of which, pursuant to section 251(f) of this chapter, no vote of the stockholders of the corporation is required); (y) a sale, lease, exchange, mortgage, pledge, transfer or other disposition (in one transaction or a series of transactions), whether as part of a dissolution or otherwise, of assets of the corporation or of any direct or indirect majority-owned subsidiary of the corporation (other than to any direct or indirect wholly-owned subsidiary or to the corporation) having an aggregate market value equal to 50% or more of either the aggregate market value of all of the assets of the corporation determined on a consolidated basis or the aggregate market value of all the outstanding stock of the corporation; or (z) a proposed tender or exchange offer for 50% or more of the outstanding voting stock of the corporation. The corporation shall give not less than 20 days notice to all interested stockholders prior to the consummation of any of the transactions described in clauses (x) or (y) of the second sentence of this paragraph.

Notwithstanding paragraphs (1), (2), (3) and (4) of this subsection, a corporation may elect by a provision of its original certificate of incorporation or any amendment thereto to be governed by this section, provided that any such amendment

to the certificate of incorporation shall not apply to restrict a business combination between the corporation and an interested stockholder of the corporation if the interested stockholder became such prior to the effective date of the amendment.

(c) As used in this section only, the term:

(1) "affiliate" means a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, another person.

(2) "associate," when used to indicate a relationship with any person, means (i) any corporation or organization of which such person is a director, officer or partner or is, directly or indirectly, the owner of 20% or more of any class of voting stock, (ii) any trust or other estate in which such person has at least a 20% beneficial interest or as to which such person serves as trustee or in a similar fiduciary capacity, and (iii) any relative or spouse of such person, or any relative of such spouse, who has the same residence as such person.

(3) "business combination," when used in reference to any corporation and any interested stockholder of such corporation, means:

(i) any merger or consolidation of the corporation or any direct or indirect majority-owned subsidiary of the corporation with (A) the interested stockholder, or (B) with any other corporation if the merger or consolidation is caused by the interested stockholder and as a result of such

merger or consolidation subsection (a) of this section is not applicable to the surviving corporation;

(ii) any sale, lease, exchange, mortgage, pledge, transfer or other disposition (in one transaction or a series of transactions), except proportionately as a stockholder of such corporation, to or with the interested stockholder, whether as part of a dissolution or otherwise, of assets of the corporation or of any direct or indirect majority-owned subsidiary of the corporation which assets have an aggregate market value equal to 10% or more of either the aggregate market value of all the assets of the corporation determined on a consolidated basis or the aggregate market value of all the outstanding stock of the corporation;

(iii) any transaction which results in the issuance or transfer by the corporation or by any direct or indirect majority-owned subsidiary of the corporation of any stock of the corporation or of such subsidiary to the interested stockholder, except (A) pursuant to the <sup>exchange</sup> exercise of warrants or ~~rights to purchase stock offered or distributed~~, or a dividend or distribution paid or made, <sup>or the exercise, exchange or conversion of</sup> pro rata to all holders of a class or series of stock of such corporation, (B) pursuant to the exercise, exchange or conversion of securities exercisable for, exchangeable for or convertible into stock of such corporation or any such subsidiary which securities were outstanding prior to the time that the interested stockholder became such, (C) pursuant to an exchange offer by the corporation to purchase

Subsequent to the time the interested stockholder became such

of securities exercisable for exchangeable for or convertible into stock of such corporation or any such subsidiary which security is distributed

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stock of the same class or series made on the same terms to all holders of said stock or (D) any issuance or transfer of stock by the corporation, provided however, that in no case under <sup>B</sup>(A-D) above shall there be an increase in the interested stockholder's proportionate share of the stock of any class or series of the corporation or of the voting stock of the corporation; ✓

A and C  
(iv) any transaction involving the corporation or any direct or indirect majority-owned subsidiary of the corporation which has the effect, directly or indirectly, of increasing the proportionate share of the stock of any class or series, or securities convertible into the stock of any class or series, of the corporation or of any such subsidiary which is owned by the interested stockholder, except as a result of immaterial changes due to fractional share adjustments or as a result of any purchase or redemption of any shares of stock not caused, directly or indirectly, by the interested stockholder; or

(v) any receipt by the interested stockholder of the benefit, directly or indirectly (except proportionately as a stockholder of such corporation) of any loans, advances, guarantees, pledges, or other financial benefits (other than those expressly permitted in subparagraphs (i)-(iv) above) provided by or through the corporation or any direct or indirect majority owned subsidiary.

(4) "control," including the term "controlling," "controlled by" and "under common control with," means the

possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting stock, by contract, or otherwise. A person who is the owner of 20% or more of a corporation's outstanding voting stock shall be presumed to have control of such corporation, in the absence of proof by a preponderance of the evidence to the contrary. Notwithstanding the foregoing, a presumption of control shall not apply where such person holds voting stock, in good faith and not for the purpose of circumventing this section, as an agent, bank, broker, nominee, custodian or trustee for one or more owners who do not individually or as a group have control of such corporation.

(5) "interested stockholder" means any person (other than the corporation and any direct or indirect majority-owned subsidiary of the corporation) <sup>T</sup> that (i) is the owner of 15% or more of the outstanding voting stock of the corporation, or (ii) is an affiliate or associate of the corporation <sup>T</sup> and was the owner of 15% or more of the outstanding voting stock of the corporation at any time within the 3-year period immediately prior to the date on which it is sought to be determined whether such person is an interested stockholder; and the affiliates and associates of such person; provided, however, that the term "interested stockholder" shall not include <sup>(x)</sup> any person <sup>(x)</sup> who (A) owned shares in excess of the 15% limitation set forth herein as of, or acquired such shares pursuant to a tender offer

commenced prior to, \_\_\_\_\_, 198\_ or pursuant to an exchange offer announced prior to the aforesaid date and commenced within 90 days thereafter and continued to own shares in excess of such 15% limitation or would have but for action by the corporation or (B) acquired said shares from a person described in (A) above by gift, inheritance or in a transaction in which no consideration was exchanged; or (y) <sup>any person</sup> whose ownership of shares in excess of the 15% limitation set forth herein is the result of action taken solely by the corporation provided that such person shall be an interested stockholder if thereafter he acquires additional shares of voting stock of the corporation, except as a result of further corporate action not caused, directly or indirectly, by such person. For the purpose of determining whether a person is an interested stockholder, the voting stock of the corporation deemed to be outstanding shall include stock deemed to be owned by the person through application of paragraph (8) of this subsection but shall not include any other unissued stock of such corporation which may be issuable pursuant to any agreement, arrangement or understanding, or upon exercise of conversion rights, warrants or options, or otherwise.

(6) "person" means any individual, corporation, partnership, unincorporated association or other entity.

(7) "voting stock" means stock of any class or series entitled to vote generally in the election of directors.

(8) "owner," including the terms "own" and "owned", when used with respect to any stock means a person that



individually or with or through any of its affiliates or associates:

(i) beneficially owns such stock, directly or indirectly; or

(ii) has (A) the right to acquire such stock (whether such right is exercisable immediately or only after the passage of time) pursuant to any agreement, arrangement or understanding, or upon the exercise of conversion rights, exchange rights, warrants or options, or otherwise; provided, however, that a person shall not be deemed the owner of stock tendered pursuant to a tender or exchange offer made by such person or any of such person's affiliates or associates until such tendered stock is accepted for purchase or exchange; or (B) the right to vote such stock pursuant to any agreement, arrangement or understanding; provided, however, that a person shall not be deemed the owner of any stock because of such person's right to vote such stock if the agreement, arrangement or understanding to vote such stock arises solely from a revocable proxy or consent given in response to a proxy or consent solicitation made to 10 or more persons; or

(iii) has any agreement, arrangement or understanding for the purpose of acquiring, holding, voting (except voting pursuant to a revocable proxy or consent as described in item (B) of clause (ii) of this paragraph), or disposing of such stock with any other person that beneficially owns, or whose affiliates or associates beneficially own, directly or indirectly, such stock.

(d) No provision of a certificate of incorporation or bylaw shall require, for any vote of stockholders required by this section, a greater vote of stockholders than that specified in this section.

(e) The Court of Chancery is hereby vested with exclusive jurisdiction to hear and determine all matters with respect to this section.



## SYNOPSIS

Section 203 is intended to strike a balance between the benefits of an unfettered market for corporate shares and the well documented and judicially recognized need to limit abusive takeover tactics. To achieve this end, the statute will delay for three years business combinations with acquirors not approved by the board unless the acquiror is able to obtain in his offer 85% of the stock as defined in the statute. This provisions is intended to encourage a full and fair offer. Following the principles of corporate democracy, two-thirds of the stockholders other than the acquiror may vote to exempt a given business combination from the restrictions of the statute. Any corporation may decide to opt out of the statute within 90 days of enactment by action of its board or, at any time, by action of its stockholders. The effect of stockholder action in this regard is delayed for 12 months to avoid circumvention of the statute.

The statute is not intended to alter the case law development of directors' fiduciary duties of care and loyalty in responding to challenges to control or the burden of proof with regard to compliance with those duties. Nor is the statute intended to prevent the use of any other lawful defensive measure.