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September 14, 1987

MEMORANDUM

TO: Michael D. Goldman
Donald J. Wolfe, Jr.
Bruce M. Stargatt
Henry N. Herndon, Jr.
Michael Hanrahan
Charles S. Crompton, Jr.
Lewis S. Black, Jr.

FROM: A. Gilchrist Sparks, III

RE: Takeover Legislation Subcommittee

Enclosed for consideration at our meeting to be held on Wednesday, September 16, are the following:

1. My initial attempt at a redrafting of proposed § 151.

2. A revised version of the § 212 proposal prepared initially by Dave Drexler.

3. A memorandum prepared at my request by Bob Valahura, an associate in our office, analyzing the constitutional issues raised by the § 151 proposal. In that connection, you should note that I asked Bob to analyze the form of the proposal forwarded with this memorandum, not the

form of proposal as initially submitted to the Section by the Secretary of State. In forwarding this memo to you at this time, I note that I have not had sufficient time to determine whether I necessarily agree with all of the conclusions reached in the memo. However, I did find it very helpful in framing the constitutional issues for further thought and consideration.

4. A recent article in The Review of Securities & Commodities Regulation analyzing the constitutionality of the New York form of statute after CTS.

/lrg
Enclosures

cc: Richard L. Templeton

ACS
draft
9/5/87

Section 151

* * *

(c) Unless otherwise restricted by the certificate of incorporation, all, but not less than all, stock held by a 10% Stockholder in excess of such 10% level, if such stock was acquired within the 12 months preceding a redemption determination with respect to such holder's stock, may be redeemed by the corporation if the board of directors determines in good faith, and based on all material facts reasonably available, that the ownership of the corporation's stock by such stockholder (i) is causing or will cause a material adverse effect (including, but not limited to, loss or threat of loss of any license or franchise from a governmental agency to conduct business, loss or threat of loss of any membership in a national securities exchange, impairment of relationships with customers, or impairment of the corporation's ability to maintain its competitive position) on the business of the corporation and its subsidiaries, or (ii) is otherwise contrary to the best [long-term] interests of the corporation or its stockholders. Notwithstanding the foregoing, a corporation shall not redeem any stock pursuant to this section until the expiration of 15 business days after the corporation gives written notice to the 10% Stockholder of the determination to redeem the stock held by such 10% Stockholder pursuant to this section. The notice shall be sent by certified or registered mail, return receipt requested, addressed to the stockholder at his address as it appears on the records of the corporation. Further, a corporation shall not redeem any stock pursuant to this section if the corporation receives from such 10% Stockholder within ten business days of such stockholder's receipt of notice, a written certification that such stockholder intends to take action which will result in such stockholder no longer holding 10% or more of the outstanding stock of the corporation entitled to vote in the election of directors and such action is taken within 30 days after the corporation's receipt of such written certification.

This section shall not apply to, and no power to redeem pursuant to this section shall be conferred on, any corporation having fewer than 300 holders of its voting stock. This section shall not apply to, and no power to redeem pursuant to this section shall be conferred with respect to, any stock acquired pursuant to a tender offer for all outstanding stock of a corporation entitled to vote in the election of directors.

Any stock redeemed pursuant to this section may be redeemed only for cash for a redemption price equal to the price per share paid for all of the redeemed stock multplied by the number of shares redeemed.

Shares which have been called for redemption pursuant to this subsection shall not be deemed to be outstanding shares for the purpose of voting or determining the total number of shares entitled to vote on any manner on and after the date on which written notice of redemption has been sent to holders thereof and a sum sufficient to redeem such shares has been irrevocably deposited or set aside to pay the redemption price to the holders of the shares upon surrender of certificates therefor; provided, however, that such shares shall have voting rights once action is taken by a 10% Stockholder disposing of such shares in accordance with this subsection, in which case the funds set aside to redeem such shares shall be returned to the corporation. In determining the sum sufficient to redeem shares pursuant to this subsection, the directors shall be entitled to rely in good faith upon public information available as to the number of shares held by a 10% Stockholder and the prices paid for such shares.

For purposes of this section, the term "voting stock" means stock entitled to vote generally for the election of directors.

For purposes of this section a "10% Stockholder" shall mean a person, corporation or entity, or a group acting in concert, who or which, together with its affiliates, is the beneficial owner of 10% or more of the outstanding voting stock of the corporation. Beneficial ownership includes, without limitation, having the right to acquire voting stock.

On the application of the corporation or any of its stockholders, the Court of Chancery is vested with exclusive jurisdiction to determine in a summary proceeding issues arising from actions taken pursuant to this section.

This Act shall be effective as to all shares acquired on or after [   ], unless the acquisition is made with the consent of the corporation.

PROPOSED ANTI-TAKEOVER STATUTE

(Section 212(b))
(Present (b) and (c) to be renumbered)

(b) A. This Section shall apply to all corporations whose voting shares are beneficially held by more than 300 persons, unless its certificate of incorporation provides otherwise.

B. For purposes of this Section:

(1) "Excess Shares" means all shares of voting stock held by a Stockholder having in excess of 10% of the total voting power of the corporation's outstanding stock of all classes with respect to the election of directors generally, except Excess Shares shall not include (i) shares acquired prior to __________, 1987; (ii) shares acquired pursuant to a tender offer made for any and all shares of a corporation's outstanding voting common stock; (iii) shares acquired prior to the time that the shares of the corporation were held by more than 300 persons; (iv) shares acquired with the consent of the corporation; (v) shares which were not Excess Shares when acquired but became Excess Shares by reason of a decrease in the number of outstanding shares of the corporation resulting from the acquisition by the corporation of voting shares from other stockholders or otherwise; or (vi) shares which are no longer Excess Shares by reason of having become eligible to vote under Paragraph C hereof.

(2) "Stockholder" shall mean, not only a stockholder of record, but also any person, corporation, other entity, or group acting in concert, who or which is the beneficial owner of the outstanding voting common stock of the corporation. Beneficial ownership includes, without limitation, having the right to acquire outstanding voting stock, but shall not include the right to vote stock pursuant to revocable proxies. "Stockholder" shall not mean any stockholder of record who certifies to the corporation that it is a nominee only, without either beneficial interest in or discretion to vote the shares which it holds of record.

C. Excess Shares shall be ineligible to vote for the removal or election of directors or the amendment of the corporation's by-laws until the third annual meeting following the acquisition of such Excess Shares, but shall be eligible to vote on all other resolutions presented to stockholders at stockholder meetings or otherwise; provided, however, that once Excess Shares have become eligible to vote for any reason, such shares shall no longer be Excess Shares and shall be disregarded in computing the number of Excess Shares owned by a Stockholder.

E. The Court of Chancery is vested with exclusive jurisdiction to deal summarily with questions arising under this Section and all persons who acquire Excess Shares shall by the act of acquisition be deemed to have consented to the jurisidction of said court for purposes of this Section only, and to have appointed the Secretary of State as his agent for service of process in accordance with Section 3104 of Title 10, or such equivalent provisions which may hereafter be enacted.

M E M O R A N D U M

TO: Corporate Law Section of the Delaware Bar Association

FROM: A. Gilchrist Sparks, III

DATE: September 14, 1987

RE: Analysis of the Revision of Section 151(c) of the General Corporation Law of the State of Delaware: The Selective Stock Redemption Provision

I. Background

State regulation of takeovers. Generally, the early or "first generation" state takeover statutes applied to tender offers for corporations incorporated under the regulating state's laws, and many of these statutes also applied to offers for corporations having substantial assets or a principal place of business in the regulating state. In addition, these statutes contained pre-offer notification requirements, waiting periods, hearing provisions and fairness determinations. Thus, these state statutes' provisions were more extensive than those contained in the federal Williams Act. In June 1982, the Supreme Court in Edgar v. MITE Corp. held that one such statute, the Illinois Business Takeover Act, was unconstitutional under the Commerce Clause. As a result of the MITE decision, states enacted a "second generation" of takeover statutes, and the Supreme Court, in CTS Corp. v. Dynamics Corp. of America, has recently held that one of these statutes, the Indiana Control Share Acquisition Act, is constitutional under both the Supremacy Clause and the Commerce

Clause. In response to the inquiry as to whether a Delaware takeover statute is desirable, the attached amendment to Section 151 has been proposed for consideration.

II. Questions Presented

Whether the proposed selective stock redemption provision to the General Corporation Law of the State of Delaware is preempted by the Williams Act or whether the provision violates either the Federal Constitution's Commerce Clause or Due Process Clause.

III. Brief Answer

The proposed stock redemption provision should be found to be constitutional under the holding in CTS Corp. v. Dynamics Corp. of America. The provision is not pre-empted by the Williams Act since it does not frustrate the purposes of the Act. Additionally, the proposed provision neither discriminates nor adversely affects interstate commerce, and the provision does not unconstitutionally hinder tender offers. Consequently, the provision does not place an unconstitutional burden of interstate commerce. Moreover, under the holding in CTS, the Court implicitly approved a similar albeit less restrictive redemption scheme in the Indiana CSA statute. Consequently, given this and the above findings, the proposed redemption provision should be found to be constitutional based upon both the Supremacy and Commerce Clauses.

As for the constitutionality of the provision under the Due Process Clause, the proposed redemption provision provides for payment for the redeemed shares at an average price. The provision, as drafted, does not ensure that the compensation will be fair and just. A Court will probably determine that since this proposed redemption provision is analogous to the eminent domain power, just compensation must be paid. Consequently, the provision must include some determination for redemption at a fair price.

IV. Details of the Proposed Stock Redemption Provision

The basic goal of this selective stock redemption provision would appear to be to reduce the threat of partial tender offers and market acquisition programs which result in the acquisition of control without giving all stockholders an opportunity to realize a fair price for their stock. This goal is accomplished by allowing the board of directors of a corporation, in its discretion, to redeem stock of a 10% stockholder which is defined as stockholder(s) who own(s) or beneficially own(s) more than 10% of the company's stock. In order to redeem the stock, however, the board of directors must make either of two findings. The board of directors must in good faith and based upon all material facts available determine either that (1) the 10% stockholder's ownership of the stock will cause a material adverse effect on the business or its subsidiaries or (2) the 10% stockholder's ownership of the stock is contrary to the best interests of the corporation or its stockholders. Thus, if the board, acting with the requisite good faith and with knowledge of all material facts reasonably available, determines that ownership by a 10%

shareholder will have a detrimental effect or will be against the best interests of the corporation, then the board may proceed with the stock redemption.

This proposed provision would be an inherent power of the corporation unless the corporation specifically takes some action to exclude this provision from the certificate. Thus, if not restricted, all the corporation must do to invoke the redemption provision is to give written notification to the 10% stockholder and to wait 15 business days from the date of the notification before commencing the stock redemption. The redemption procedure is placed on hold, however, by what could be called a "back down" provision. This provision states that if the 10% stockholder notifies the corporation by written certification that his holdings will go back down to or below 10% ownership level, the corporation may not redeem the stock. The 10% shareholder then has 30 days from the receipt of the back down notice by the corporation to divest himself of all stock in excess of 10%. If the 10% stockholder fails to do this, the corporation may, after the expiration of the 30 days, immediately redeem his stock.

When redemption is approved and the above procedures are complied with, the provision allows a corporation's board of directors to redeem all stock in which a 10% stockholder has over 10%, but the corporation may not redeem the 10% stockholder's stock below the 10% ownership level. The only stock that may be redeemed, however, must have been acquired within the preceding 12 months from the time the corporation notifies the 10% shareholder of its intention to redeem the stock. It should be noted that the proposed provision contains no prohibition against a 10% shareholder reacquiring additional shares after his shares have been redeemed. Furthermore, as for the payout for the redeemed stock, the proposed provision mandates that the shares be bought at an average price paid for all redeemed shares and that the redeemable stock must be paid for in cash.[1] Once both the excess shares over 10% are called for redemption and the corporation has set aside money sufficient to redeem those shares, the shares may not be voted. The shares regain their ability to be voted, however, when the shares are disposed of by the 10% stockholder, but if the shares are redeemed, the corporation may not vote them.

In addition to the director's discretion not to redeem stock, the provision may be rendered inapplicable in other ways. The most notable way is the tender offer for all shares. As long as the tender offer includes an offer for all shares, the corporation, under this provision, has no power to redeem the 10% stockholder/offeror's shares. This provision appears to make difficult the coercive two-tier tender offer by forcing the acquiror either to bid for all the shares if the takeover is hostile or, if the offer is less than for all

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1 The original version submitted to the Section provided for a fair price with an average price cap. Analytically, this formulation is no better from a due process point of view than that contained in the present draft of the statute, since it still permits redemption for less than a fair price.

the shares, to face the board which would then have a redemption option under this provision. Additionally, the statute does not apply to corporations that are not widely owned by a number of stockholders: For the statute to apply, the stock must be owned by at least 300 shareholders.

V. Discussion

As an overview to the analysis of the constitutionality of this provision, it should be noted that the Indiana Control Share Acquisition "CSA" Statute upheld by the Supreme Court in CTS Corp. v. Dynamics Corp. of America, ___ U.S. ___, 107 S. Ct. 1637 (1987), contained a redemption provision. Basically, the redemption provision in the CSA statute allows the corporation to redeem the shares of a 20% stockholder. The full text of the redemption provision under the Indiana CSA statute is set out in full here to allow comparison:

> [REDEMPTION]. - (a) If authorized in a corporation's articles of incorporation or bylaws before a control share acquisition has occurred, control shares acquired in a control share acquisition with respect to which no acquiring person statement has been filed with the issuing public corporation may, at any time during the period ending sixty (60) days after the last acquisition of control shares by the acquiring person, be subject to redemption by the corporation at the fair value thereof pursuant to the procedures adopted by the corporation.
>
> (b) Control shares acquired in a control share acquisition are not subject to redemption after an acquiring person statement has been filed unless the shares are not accorded full voting rights by the shareholders as provided in section 9 of this chapter.

Indiana Business Corporation Law § 23-1-42-10 (Supp. 1986). Generally, the statute provides for redemption by the corporation at any time up until 60 days after the final control share stock acquisition was made only when an acquiring person statement (a general information and disclosure statement) has not been filed. If an acquiring person statement has been filed, the corporation may only redeem the stock if the stockholders do not vote to restore voting rights to the shares.

As laid out above, the Indiana CSA redemption provision seems to give a free hand to the corporation as to the circumstances of redemption. Except for the 60-day limitation, the failure to file an acquiring person statement and the at least 20% ownership level needed to make a control share acquisition, there is no limitation on the corporation's power to redeem. Indeed, unlike in the proposed provision, the board under the CSA statute appears to have unfettered discretion. It would seem, however, that a court interpreting this provision, to avoid problems such as entrenchment motives, would impose a good faith requirement on the corporation. <u>See</u>, <u>e.g.</u>, <u>Unocal Corp. v. Mesa Petroleum</u>, Del. Supr., 493 A.2d 946 (1985). This presumably would be similar to the requirements imposed by the proposed selective redemption provision.

An area in which there are differences between these provisions is that the CSA provision is intertwined with a much larger statutory scheme. A court could find that this type of redemption provision would only be constitutional if construed together with the other provisions of a CSA statute. Indeed, a bald-faced redemption provision which contains no method for shareholder participation may be found unconstitutional if it were not included as part of a larger act. The fact that under the proposed provision offers for all shares are still unregulated suggests that this might be an important factor, and this is discussed further in the following sections. Moreover, another difference here is that the CSA statute requires a fair market value redemption price and the proposed provision requires an average price redemption. This is an important distinction and one which is discussed in detail in Section V. C. below.

Whether these differences would be enough to force the Court to find unconstitutional this proposed redemption provision is subject to debate, but it may be argued that a redemption provision such as the one proposed here is constitutional just under the general holding in CTS. It should be remembered, however, that the Court, except for noting the existence and function of the Indiana CSA act redemption provision, did not directly address the constitutionality of that provision. Thus, to rely directly on the CTS holding for the proposition that this proposed provision is constitutional would be unwise.

Before looking at the specific analysis in CTS, one additional aspect of the Court's decision in that case should be considered. Throughout the opinion there is a continuing discussion and reliance on the effect of shareholder participation. The Court in both the analysis of the Commerce Clause issues and the pre-emption issues repeatedly mentioned the direct role that the shareholders play under the Indiana CSA Act. In a number of instances, this shareholder participation seems to be the touchstone that the Court was looking to, and it may be that it was the key to the constitutional viability of this statute. If so, any statute, which might include the one proposed, that doesn't focus on shareholder participation might be found to be unconstitutional. Where relevant, the effect of shareholder participation is discussed in the following sections.

A. Supremacy Clause: Pre-emption by the Williams Act

Under the Supremacy Clause of the United States Constitution, in cases in which Congress has not completely displaced state regulation of a specific area, state legislation is void to the extent it actually conflicts with federal law. As the Supreme Court noted in CTS, absent an explicit indication by Congress of an intent to pre-empt state law, a state statute is pre-empted only "where compliance with both federal and state regulations is a physical impossibility . . . or where the state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." CTS, 107 S. Ct. at 1644, quoting Florida Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 137, 142-143 (1963) and Hines v. Davidowitz, 312 U.S. 52, 67 (1941). Because it is entirely possible to be in compliance with both the Williams Act and the redemption provision, the proposed provision can be pre-empted only "if it frustrates the purposes of the federal law." CTS, 107 S. Ct. at 1644.

According to the Court, the Williams Act imposes requirements in two basic areas. First, it requires that upon commencement of the tender offer, the offeror must file statements disclosing information about the offer.[2] Second, the Williams Act, and the regulations that accompany it, establish procedural rules to govern tender offers.[3] Based on the foregoing, the Court, in the CTS case, determined that under the Williams Act a state statute cannot be adopted which operates

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2 The Williams Act establishes disclosure requirements designed to protect all shareholders of the target corporation. These disclosures include: the offeror's background and identity; the source and amount of the funds to be used in making the purchase; the purpose of the purchase, including any plans to liquidate the company or make major changes in its corporate structure; and the extent of the offeror's holdings in the target company. See 15 U.S.C. § 78n(d)(1) (incorporating § 78m(d)(1) by reference); 17 CFR §§ 240.13d-1, 240.14d-8 (1986). CTS, 107 S. Ct. at 1644.

3 The Act guarantees certain rights to those shareholders of the target corporation who elect to tender their stock. For example, stockholders who tender their shares may withdraw them during the first 15 business days of the tender offer and, if the offeror has not purchased their shares, any time after 60 days from commencement of the offer. 15 U.S.C. § 78n(d)(5); 17 CFR § 240.14d-7(a)(1) (1986). The offer must remain open for at least 20 business days. 17 CFR § 240.14e-1(a) (1986). If more shares are tendered than the offeror sought to purchase, purchases must be made on a pro rata basis from each tendering shareholder. 15 U.S.C. § 78n(d)(6); 17 CFR § 240.14(8) (1986). Finally, the offeror must pay the same price for all purchases; if the offering price is increased before the end of the offer, those who already have tendered must receive the benefit of the increased price. § 78n(d)(7). CTS, 107 S. Ct. at 1644.

"to favor management against offerors, to the detriment of shareholders." CTS, 107 S. Ct. at 1645. The Court, focusing on the conflict between the corporation and the offeror, indicated that the statute should protect the "independent shareholder" against the corporation and the offeror by furthering a basic purpose of the Williams Act by "placing investors on an equal footing with the takeover bidder." CTS, 107 S. Ct. at 1645-46.

In applying these concepts to the Indiana CSA Act, the Court focused on several aspects of the statute which the Court determined made it consistent with the Williams Act. The Court highlighted the following issues regarding the CSA statute:

1. Whether independent shareholders faced with a tender offer are placed at a disadvantage because of the CSA statute;

2. Whether the CSA statute allows state government to interpose views of fairness between willing buyers and sellers of shares of the target or whether it allows shareholders to evaluate the fairness of offer collectively;

3. Whether the CSA statute could cause any possible problems of communication of the offer to shareholders; and

4. Whether the CSA statute causes impermissible delays in the implementation of tender offers.

Regarding the first issue, the Court deemed the equality of the CSA statute's impact on independent shareholders just as important as the impact on either management or the offeror. In finding that the CSA statute allows shareholders to vote as a group, the Court determined that the shareholders are protected from the coercive aspects of some tender offers. This proposed redemption provision could be seen as being equally in favor of the shareholders in that one of the expressed intents of this provision is to protect shareholders by deterring potentially coercive two-tier tender offers or unfair market acquisition programs. Moreover, the provision still ensures that shareholders, acting as a group, may accept or reject a tender offer for all shares. The desire to protect shareholders of Delaware corporations from "this type of coercive offer does not conflict with the Williams Act. Rather, it furthers the federal policy of investor protection." CTS, 107 S. Ct. at 1646.

Secondly, the proposed provision has no built-in method designed to impose state government views of fairness of offers, but a major concern regarding this proposed redemption provision is that shareholders, unlike in the CSA statute, may not always participate directly in the determination of the fairness of an offer. Under the CSA Act, the acquisition of control of a corporation is conditioned upon approval of a majority of the pre-existing disinterested shareholders. Except for an offer for all shares, the proposed redemption provision leaves this determination to the discretion of the board of directors allowing the board to substitute its decision on the fairness of the offer for the shareholder's decision. Since shareholders could be prevented from consideration of partial tender offers, the Court may be inclined to review this as a tipping of the scales in favor of management. The Court would probably find, however, that since this provision was proposed to "protect investors" and since shareholder review of an offer for all shares has not been affected or changed, any concerns regarding quantity of shareholder participation would not be material.

Additionally, as with the CSA statute, the proposed redemption provision does nothing to change or hinder the means of communicating offers to the shareholders, and, as such, it is not a problem in regard to concerns outlined in CTS or the MITE case. Finally, the Court discussed at length the delay provisions in the CSA Act and determined that the statute did nothing to impose an unreasonable delay in the making of tender offers. Here, the language of the proposed redemption provision imposes no delay as to when an offer can be made. There are no time restrictions on offers involved and, indeed, an offer for all shares is specifically left unrestricted by the provision. Consequently, this major concern raised in CTS does not present any difficulties for this proposed provision.

Under this proposed redemption provision, stockholders are not faced with delays in the communication or implementation of a tender offer, and they are not placed at a disadvantage when presented with the offer. Based upon these reasons and the fact that this provision seeks to protect shareholders from the effects of coercive offers, does nothing to directly prevent tender offers, and still provides a means for shareholder participation, the proposed selective stock redemption provision does not appear to conflict with the text or to frustrate the purposes of the Williams Act. Thus, the proposed provision should be valid under the Supremacy Clause.

B. Commerce Clause

The Commerce Clause provides that "Congress shall have power . . . [t]o regulate Commerce . . . among the several States." U.S. Const., Art. I, § 8, cl. 3. Over the years, the Supreme Court has "articulated a variety of tests in an attempt to describe the difference between those regulations that the Commerce Clause permits and those regulations that it prohibits." CTS, 107 S. Ct. at 1648. In looking at the Commerce Clause issue, the Court in CTS outlined three areas of concern: (1) State statutes that discriminate against interstate commerce; (2) State statutes that adversely affect interstate commerce by subjecting activities to inconsistent regulations; and (3) State statutes that potentially hinder tender offers.

As for the discriminatory effects on interstate commerce, the point on which the Court upheld the Indiana CSA Act was the requirement that a statute have "the same effects on tender offers whether or not the offeror is a domiciliary or resident of [the regulating state]." CTS, 107 S. Ct. at 1648-49. In addition, the Court rejected the contention that the CSA statute is discriminatory because it will apply more often to out-of-state corporations. This, the Court determined, would not, by itself, establish a claim of discrimination against interstate commerce. Under the proposed redemption provision, the domicile of the offeror/10% shareholder plays no role in the operation of the provision. The effect on offers is the same on Delaware corporations or individuals as that on out-of-state corporations or individuals. Indeed, the provision "visits its effects equally upon both interstate and local business." CTS, 107 S. Ct. at 1649. Hence, the proposed provision will not impose a greater burden on out-of-state offerors than it will on Delaware offerors, and the Court will conclude that this provision would not discriminate against interstate commerce.

In discussing the possibility that the Indiana CSA statute may adversely affect interstate commerce by subjecting corporate activities to inconsistent regulations by different states, the Court in CTS explained that so long as each state regulates the voting rights of corporations that it had created, the corporation will only be subject to the law of one state. Furthermore, the Court stated "[n]o principle of corporation law and practice is more firmly established than a state's authority to regulate domestic corporations, including the authority to define voting rights of shareholders." CTS, 107 S. Ct. at 1649. As noted above, this proposed redemption provision would be an inherent power of a Delaware corporation subject only to the restrictions of the company's own certificate of incorporation. Since this proposed provision would only apply to corporation's incorporated under the laws of

Delaware, this provision would not subject the corporation to a risk of impermissible regulation by differing states.

Finally, the Court was faced with determining whether the Indiana CSA statute unconstitutionally interfered with tender offers. The Court described the nature of corporation governance by the states and discussed some of the traditional regulations which affect resident and non-resident shareholders of a corporation. The Court noted that it is "an accepted part of the business landscape in this country for States to create corporations, to prescribe their powers, and to define the rights that are acquired by purchasing their shares." CTS, 107 S. Ct. at 1650. This seems to be the strongest language in support of this proposed redemption provision since this proposed provision would be defining the right of a shareholder as to his shares.

The Court went on to state that "[a] state has an interest in promoting stable relationships among parties involved in the corporations it charters, as well as in ensuring that investors in such corporations have an effective voice in corporate affairs." CTS, 107 S. Ct. at 1651. The Court upheld the Indiana CSA statute since it reflected these concerns and since the statute's primary purpose was to protect the shareholders of Indiana corporations. This same reasoning applies to the proposed redemption provision. It is proposed to protect shareholders of Delaware corporations and would be "especially beneficial where a hostile tender offer may coerce shareholders into tendering their shares." CTS, 107 S. Ct. at 1651.

The most troubling Commerce Clause issue regarding this proposed provision is the Court's discussion of the jurisdictional standard upon which the CSA statute is based. An argument advanced in CTS was that the CSA statute violated the Commerce Clause since the state had no legitimate interest in protecting the non-resident shareholders. The Court "reject[ed] the contention that Indiana has no interest in providing for the shareholders of its corporations the voting autonomy granted by the Act." CTS, 107 S. Ct. at 1651. The Court here seemed to be saying that the essential jurisdictional aspect of the CSA statute was that statute must only regulate domestic corporations. Without more, this indicates that Delaware could act based on the concerns of only shareholders of Delaware corporations.

The Court went further, however, and stated that "[m]oreover, unlike the Illinois statute invalidated in MITE, the Indiana Act applies only to corporations that have a substantial number of shareholders in Indiana . . . . Thus, every application of the Indiana Act will affect a substantial number of Indiana residents, whom Indiana indisputably has an interest in protecting." CTS, 107 S. Ct. at 1652. The Court's pronouncement that this statute was additionally valid because of the number of domestic shareholders has potentially adverse repercussions for Delaware's adoption of a takeover statute. Indeed, speaking to this issue, one commentator has stated that:

> [this] leaves the Court room in the future to distinguish its holding if a state like Delaware, for example, which is the state of incorporation for a large number of corporations with a minimal number of Delaware residents as shareholders, should adopt a Control Shareholder Acquisition Act without requiring any contact with the state other than incorporation.

Bloomenthal, "Control Share Acquisitions Act," 9 Securities and Federal Corporate Law Report 44 (1987). Given this, it is unclear whether a Delaware CSA statute would be constitutionally permissible under the Commerce Clause if to obtain jurisdiction the incorporating state would need a substantial number of domestic shareholders. Based, however, upon the strong language in CTS regarding the well established right of the state to create, limit and define corporate existence, this proposed redemption power, since it is made part of the inherent power of the corporation and is well within the ambit of internal affairs, should withstand the jurisdictional requirements of the Commerce Clause.

Finally, in addressing the argument that the number of successful tender offers would be limited, the Court dismissed that issue by finding that the Indiana CSA statute would not interfere with either a resident or non-resident's offer to purchase shares or attempt to gain control. Indeed, according to the Court even if the number of takeover proposals were reduced, the Commerce Clause analysis would be the same. Since the proposed redemption provision only "provides regulatory procedures designed for better protection of the corporation's shareholder," CTS, 107 S. Ct. at 1652, and since the proposed provision does not prohibit any entity from offering to purchase, or from purchasing shares in a Delaware corporation or from attempting thereby to gain control, the Court should conclude that the proposed provision is not an unconstitutional hindrance on tender offers. Therefore, based on the fact that the proposed provision does not adversely affect interstate commerce, that it does not subject corporations to inconsistent regulations and that it does not unconstitutionally hinder tender offers, the Court would presumably uphold this provision under the Commerce Clause.

C. Due Process

The U.S. Supreme Court in CTS did not address a due process argument, and the issue here then is whether or not this proposed provision should actually be analyzed under a due process/eminent domain theory. One analogy that tends to indicate a due process review is necessary is that the stock redemption provision is similar to the forced selling of a minority shareholder's shares in a short-form merger. See 8 Del. C. § 253. Early cases regarding statutorily approved majority cash-outs of minority shareholders sustained the buy-out as an exercise in the right of eminent domain. Spencer v. Seaboard Airline R.Y. Co., 137 N.C. 107, 49 S.E. 96 (1904); Narragansett Electric Lighting Co. v. Sabre, 50 R.I. 288, 146 A. 777 (1929); see also Offield v. N.Y., New Haven, & Hartford Railroad Co., 203 U.S. 372 (1906) (The Supreme Court found that a statute authorizing purchase of shares and appraisal rights to dissenting minority stockholders when Railroad owned

75% of stock to be within the power of the state and not a violation of the 14th Amendment.). Indeed, Delaware courts have recognized that the power of a stockholder majority to override minority dissenters and remit them to the cash appraisal remedy is "analogous to the right of eminent domain." Federal United Corp. v. Havender, Del. Supr., 11 A.2d 331, 338-339 (1940); Meade v. Pacific Gamble Robinson Co., Del. Ch., 51 A.2d 313, 317 (1947), aff'd, Del. Supr., 58 A.2d 415 (1948). Thus, it would appear that analysis of the eminent domain issues would be appropriate.

There is, however, an argument that this proposed provision should be considered free from an due process/eminent domain review since it entails a private agreement between a stockholder and a corporation. For example, the short-form merger statutes have been upheld against constitutional attacks based upon due process arguments. Coyne v. Park & Tilford Distillers Corporation, Del. Supr., 154 A.2d 893 (1959) (citing Beloff v. Consolidated Edison Co. of New York, 300 N.Y. 11, 87 N.E. 2d 561 (1949)). Rather than looking at the forced redemption procedure in an eminent domain framework, the courts have upheld these statutes on the grounds that the stockholder is on notice that the statutory provisions governing the relationship between a corporation and its stockholders can be amended at any time. Coyne, 154 A.2d at 897; see 8 Del. C. §§ 242, 394. However, these decisions were made in the context of a statutory scheme that guaranteed to stockholders a fair price for their stock, poses. Kaye v. Pantone, Inc., Del. Ch., 395 A.2d 369, ___ (1975). It is, however, "dormant right lodged in the sovereign people until legislative action points out the occasions, the modes and the agencies for its exercise." Thomison v. Hillcrest Athletic Ass'n, Del. Super., 5 A.2d 236, 238 (1939). A legislature may thus determine by what agency it may wish to delegate eminent domain power, and it has been held that a legislature may delegate the power to corporations. See Greenwood v. Union Fright Railroad Co., 105 U.S. 13 (1881); see also 1A Nichols' The Law Of Eminent Domain § 3.23 (cases cited therein); Randolph v. Wilmington Housing Authority, Del. Supr., 139 A.2d 476 (1958) (Eminent Domain power given to semi-private authority). Since the power of eminent domain may not be exercised by private corporations in the absence of constitutional or statutory provisions, the legislatively delegated power given to a corporation to redeem stock under the proposed provision probably would be construed as a legitimate delegation of eminent domain power under the Due Process Clause.[4]

Property Taken Must Be For Public Use. This is potentially one of the most difficult hurdles regarding the constitutionality of this proposed provision. It is clear

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4 There may be some type of hearing mandated by due process other than the determination of the Board of Directors. See Fuentes v. Shevin, 407 U.S. 67 (1972); Formosa Plastics Corp. v. Wilson, Del. Supr., 504 A.2d 1083 (1986) ("Before a party can be deprived of life, liberty, or property, it has the right to notice and a hearing in a meaningful time and meaningful manner.").

either through the appraisal process or otherwise through Court redress. Consequently, since the proposed Section 151 provision does not guarantee that a fair price will be paid, there is a strong likelihood that a court would go on to analyze the taking under traditional eminent domain concepts.

Takings: State and Federal. The U.S. Constitution provides that "no person shall . . . be deprived of . . . property without due process of law; nor shall private property be taken for public use, without just compensation." U.S. Const. Amend. V. This amendment is applicable to the states through the 14th Amendment's Due Process Clause. Chicago B & Q. R. Co. v. Chicago, 166 U.S. 226 (1897). Moreover, the Delaware Constitution states that no person's property may be "taken or applied to public use without the consent of this representatives, and without compensation being made." Del. Const. Art. I, sec. 8. Delaware Courts have generally proceeded on the basis that both the constitutional guarantees involved here provide the same degree of protection against takings of property. See New Castle County School District v. State, Del. Supr., 424 A.2d 15 (1980). Hence, for the purposes of this proposed provision, the eminent domain issues under state and federal law are essentially the same.

Delegation of Eminent Domain Power to Private Parties. Delaware courts have held that eminent domain power is a constitutional right which is vested in the sovereign which enables it to take private property for public purposes. Kaye v. Pantone, Inc., Del. Ch., 395 A.2d 369, ___

(1975). It is, however, "dormant right lodged in the sovereign people until legislative action points out the occasions, the modes and the agencies for its exercise." Thomison v. Hillcrest Athletic Ass'n, Del. Super., 5 A.2d 236, 238 (1939). A legislature may thus determine by what agency it may wish to delegate eminent domain power, and it has been held that a legislature may delegate the power to corporations. See Greenwood v. Union Fright Railroad Co., 105 U.S. 13 (1881); see also 1A Nichols' The Law Of Eminent Domain § 3.23 (cases cited therein); Randolph v. Wilmington Housing Authority, Del. Supr., 139 A.2d 476 (1958) (Eminent Domain power given to semi-private authority). Since the power of eminent domain may not be exercised by private corporations in the absence of constitutional or statutory provisions, the legislatively delegated power given to a corporation to redeem stock under the proposed provision probably would be construed as a legitimate delegation of eminent domain power under the Due Process Clause.[4]

Property Taken Must Be For Public Use. This is potentially one of the most difficult hurdles regarding the constitutionality of this proposed provision. It is clear beyond a doubt that a state may not constitutionally condemn

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[4] There may be some type of hearing mandated by due process other than the determination of the Board of Directors. See Fuentes v. Shevin, 407 U.S. 67 (1972); Formosa Plastics Corp. v. Wilson, Del. Supr., 504 A.2d 1083 (1986) ("Before a party can be deprived of life, liberty, or property, it has the right to notice and a hearing in a meaningful time and meaningful manner.").

property for private use. Randolph v. Wilmington Housing Authority, Del. Supr., 139 A.2d 476 (1958). Property acquired in eminent domain proceedings may be only obtained for public uses or purposes, W.P.A. v. Ranken, Del. Supr., 105 A.2d 614, 630 (1954), and it is the providence of the Legislature or Congress to determine what is a public use. United States ex rel. Tennessee Valley Authority v. Welch, 327 U.S. 546 (1946); W.P.A. v. Ranken, 105 A.2d at 620. Delaware courts have determined that the phrase "'public purpose' is not susceptible of precise definition, and it is not possible to adopt any rigid rule by which to determine whether a purpose or use is to be upheld public or private." W.P.A. v. Ranken, 105 A.2d at 619.

For our purposes, it is important to note that the congressional or legislative findings on what is a public purpose is entitled to great weight. U.S. ex rel. T.V.A., 327 U.S. at 552; Randolph, 139 A.2d at 482; W.P.A. v. Ranken, 105 A.2d at 620. Although the final determination of what is a public use is ultimately a judicial question, Cincinnati v. Vester, 281 U.S. 439, 446 (1930); Wilmington Parking Authority v. Land with Improvements, Del. Supr., 521 A.2d 227, 231 (1987), the courts allow great deference to Congress and the legislature. U.S. ex rel. T.V.A., 327 U.S. at 552. Thus, unless the legislative finding is clearly unreasonable, the determination of the legislature as to what is a public use must prevail. Randolph, 139 A.2d at 482.

The difficult question regarding this proposed redemption provision then is whether the taking of the stock by the private corporation is for public use or purposes. For a court to ascertain whether a statutory authorized taking is for public purposes, there must be some sort of intent to benefit the public. The more detailed the findings and the more documented the need for the legislation, the more likely it is for a court to defer to the judgment of congress or the legislature. See, e.g., Keystone Bituminous Coal Ass'n v. DeBenedictis, ___ U.S. ___, 107 S. Ct. 1232, 1242, n.14 (1987). Delaware courts have also indicated that in determining whether the primary purpose of a project is public or private, the cases tend "to classify the object according to its primary consequences and effects." W.P.A. v. Land with Improvements, 521 A.2d at 232; Randolph, 139 A.2d at 483. Therefore, the courts will look to both the purposes and the effects of the legislatively imposed taking authority to determine whether the taking is for a public or private use.

To make more likely the finding that this proposed redemption provision is not an unconstitutional taking, the record should reflect a number of arguments which could be advanced to indicate a public purpose. For example, using some of the arguments in CTS, the legislature could determine that the redemption provision will have the effect of benefiting the public by allowing corporations and their shareholders (members of the public) to analyze and assess takeover offers more closely. Legislation such as this might also ensure that investors in corporations have an effective voice in corporate affairs, and this proposed provision may make for stable conditions within the business community. Whatever the chosen reasons, it is clear that without a well documented and reasonable public purpose, the courts could find this provision is a violation of the 14th Amendment.

Just Compensation. Of all the above eminent domain issues, the only really likely successful attack on this proposed provision will come under this issue. Delaware Courts have held that both the Federal and State Constitutions limit the right of eminent domain and that "private property may not even be taken for public use without just compensation." Thomison, 5 A.2d at 236; see also State v. Davis Concrete of Delaware, Inc., Del. Supr., 355 A.2d 883 (1976). Thus, it must be determined what "just compensation" requires. The Superior Court in the Thomison case stated that the term just compensation is "uniformly construed to mean the fair market value based on the measure of a voluntary sale by an owner willing but not obliged to sell and a purchaser willing but not obliged to buy." Thomison, 5 A.2d at 238-39; 0.744 of an Acre of Land v. State, Del. Supr., 251 A.2d 341 (1969). Therefore, it would appear that the fair market value of the property is the benchmark for just compensation. In addition, it has been held that just compensation is to be ascertained upon the basis of the fair market value of the property as of the date of the taking. Wilmington Housing Authority v. Harris, Del. Super., 93 A.2d 518 (1952).

A moment's reflection will demonstrate that the proposed redemption provision could very well cause the 10% shareholder's redeemed stock to be purchased for less than its fair market value at the time of its redemption. Consequently, based on the fact that a fair market value may not be paid, this provision does not provide for the constitutionally required just compensation, and a court would probably determine that the average price provision of the selective redemption provision will violate the Due Process Clause. If however the proposed redemption provision contained either an appraisal method provision or a fair market value provision, a Court would presumably find this acceptable under the 14th Amendment.

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STATE TAKEOVER STATUTES AFTER *MITE*

Recent Decisions Cast Doubt on the Constitutionality of Second-Generation Statutes That Limit Acquirors' Voting Rights or Other Powers. Registration and Disclosure Requirements Have Been Upheld, However, When They Protect Local Investors and Do Not Unduly Burden Offerors.

By Greg A. Danilow and Philip Bentley*

The Supreme Court's decision in *Edgar* v. *MITE Corp.*[1] sounded the death knell for the first generation of state takeover statutes. More recent decisions have laid to rest a number of second-generation state takeover statutes and suggest that the life span for less restrictive second-generation statutes such as New York's may be brief. The Supreme Court will soon have the opportunity to clarify the law in this area further when it decides *Dynamics Corp.* v. *CTS Corp.*,[2] a case in which it has just noted probable jurisdiction.

In *MITE*, the Supreme Court held that the Illinois Business Takeover Act, a typical first-generation statute, violated the Commerce Clause because it excessively burdened interstate commerce. Three justices found the Act invalid under the Supremacy Clause as well, on the ground that it undermined the policy of neutrality embodied in the Williams Act. Subsequent lower court decisions read *MITE* broadly, invalidating state takeover statutes on both Commerce Clause and preemption grounds.[3]

MITE and its progeny spawned a new generation of state takeover laws designed to avoid the constitutional infirmities of the earlier statutes. These new statutes eschew the first-generation approach of setting up a regulatory scheme to be administered by a state official; instead, they are drafted in the form of traditional state corporation laws. The most ambitious and widely copied of these second-generation statutes is Ohio's Control Share Acquisition Act (passed only months after *MITE*),[4] which requires prior shareholder approval for all acquisitions of "controlling stock interests." More recently, several states have enacted modified second-generation laws, crafted so as to skirt the principal constitutional objections to the Ohio Act. Indiana adopted a toned-down control share acquisition law, which makes an acquiror's voting rights, but not the acquisition itself, subject to shareholder approval.[5] New York's new takeover law is even less restrictive: it allows a target board merely to bar an acquiror from subsequently effecting a merger or other business combination with the target.[6]

Recent decisions have doomed the control share acquisi-

1. 457 U.S. 624 (1982).
2. 794 F.2d 250 (7th Cir. 1986), prob. juris. noted, 55 U.S.L.W. 3231 (Oct. 7, 1986).
3. See, e.g., *National City Lines* v. *LLC Corp.*, 687 F.2d 1122 (8th Cir. 1982); *Martin Marietta Corp.* v. *Bendix Corp.*, 690 F2d 558 (6th Cir. 1982). See generally Block, Barton, Roth & Garfield, *State Takeover Statutes*, in *Hostile Battles for Corporate Control* (PLI) (D. Block & H. Pitt eds. 1986).
4. Ohio Rev. Code §1701.831. Hawaii, Missouri, Minnesota, and Utah have enacted statutes closely modeled after Ohio's. Hawaii Rev. Stat. §§ 416-171, 172; Mo. Rev. Stat. § 351.407; Minn. Stat. § 302A.671; Utah Code Ann. § 64-4.1.
5. Ind. Code §§ 23-1-42-1 et seq. Wisconsin recently amended its takeover law (previously modeled after Ohio's) to follow Indiana's. Wis. Stat. § 552.
6. N.Y. Bus. Corp. Law §912. Kentucky and New Jersey recently enacted statutes similar to New York's. Ky. Rev. Stat. §§ 292.570-292.630; N.J. Rev. Stat. § 49.5-1.

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tion laws. The first blow was struck in 1985, when two federal district courts invalidated Missouri's and Minnesota's control share laws, both closely modeled after Ohio's.[7] Then, in 1986, the Sixth Circuit and a third district court struck down Ohio's and Hawaii's control share statutes.[8] And in *Dynamics,* the Seventh Circuit, in a forceful opinion by Judge Posner, invalidated Indiana's less restrictive control share act.

The constitutionality of New York's new takeover law has yet to be tested. The New York act is more carefully drafted than the control share acquisition statutes; but if the principles set forth in the recent federal decisions are followed, the New York act is not likely to survive. Only New York's disclosure provisions[9]—requiring tender offerors to file a registration statement disclosing the takeover's likely effect on state residents—are likely to withstand scrutiny.

EDGAR V. MITE CORP.

Edgar v. *MITE Corp.* arose out of a tender offer by MITE Corporation, a Delaware corporation with its principal office in Connecticut, for Chicago Rivet & Machine Co., an Illinois corporation. Instead of complying with the Illinois Business Takeover Act, MITE sought a declaratory judgment that the Illinois Act was unconstitutional, and preliminary and permanent injunctions prohibiting the enforcement of the Act. The District Court issued a preliminary injunction, and the Seventh Circuit and a divided Supreme Court affirmed.

The Illinois Act was typical of the first generation of takeover statutes. It required a tender offeror to notify the Illinois Secretary of State and the target company of its intent to make a tender offer, and of the terms of the offer, 20 days before the offer became effective. During that time, the offeror could not communicate its offer to the stockholders, but the target company was free to disseminate information about the offer to its stockholders. In addition, the statute allowed the secretary of state to call a hearing at any time during the 20-day waiting period, and required a hearing if requested by the target's outside directors or its shareholders. Finally, the statute directed the secretary of state to refuse to register the tender offer (thereby blocking it) if he found that the offer was inequitable or that the offeror's disclosure materials were inadequate.

The Supreme Court's decision to strike down the Illinois Act was unusually fragmented, with six separate opinions. A majority of the Court adopted only part of Justice White's five-part opinion, holding that the Illinois Act violated the Commerce Clause because it excessively burdened interstate commerce. In addition, three justices joined Justice White in finding the Act unconstitutional as a direct regulation of interstate commerce. Finally, two justices joined Justice White in finding the Act preempted by the Williams Act and therefore violative of the Supremacy Clause.

In holding the Illinois Act unconstitutional as an excessive burden on interstate commerce, the Court emphasized that the statute allowed the Illinois Secretary of State to block nationwide tender offers—either by delaying an offer excessively (thus giving target management time to implement defensive measures or find a friendly suitor), or by refusing to register an offer. The Act thereby heavily burdened interstate commerce:

> Shareholders are deprived of the opportunity to sell their shares at a premium. The reallocation of economic resources to their highest valued use, a process which can improve efficiency and competition, is hindered. The incentive the tender offer mechanism provides incumbent management to perform well so that stock prices remain high is reduced.[10]

The Court rejected Illinois' contention that these burdens were offset by the Act's benefits to Illinois shareholders, concluding that any such benefits were "for the most part, speculative." Finally, the Court rejected Illinois' contention that the statute merely regulated the internal affairs of Illinois corporations, noting that "[t]ender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company."

Four justices found the Illinois Act unconstitutional also as a direct regulation of interstate commerce. Justice White (joined on this issue by Justices Burger, Stevens, and O'Connor) noted in particular that the Illinois law was not limited to transactions involving Illinois shareholders; the law "would apply even if not a single one of Chicago Rivet's shareholders were a resident of Illinois."

Finally, three justices (White, Burger, and Blackmun) found the Illinois Act invalid under the Supremacy Clause

7. *Icahn* v. *Blunt*, 612 F. Supp. 1400 (W.D. Mo. 1985); *APL Ltd. Partnership* v. *Van Dusen Air, Inc.*, 622 F. Supp. 1216 (D. Minn. 1985).
8. *Fleet Aerospace Corp.* v. *Holderman*, 796 F.2d 135 (6th Cir. 1986); *Terry* v. *Yamashita*, CCH ¶ 92,745 (D. Hawaii 1986).
9. N.Y. Bus. Corp. Law §§1600-1613.
10. 457 U.S. at 643.

as well, because it conflicted with the objectives of the Williams Act. Justice White's opinion stated that, although Congress did not intend the Williams Act to preempt the takeover field absolutely, the Williams Act does embody certain policies—neutrality and investor autonomy—that the states are not free to frustrate. The Illinois law undermined both of these policies. By allowing the Illinois Secretary of State to delay and even block tender offers, the law upset the careful balance struck by Congress between target management and bidders and deprived investors of the opportunity to tender their shares into hostile offers.

In separate concurrences, Justices Powell and Stevens joined the majority's holding that the Illinois Act excessively burdened interstate commerce, but disagreed with the plurality's preemption analysis. Justice Powell wrote:

> I agree with Justice Stevens that the Williams Act's neutrality policy does not necessarily imply a congressional intent to prohibit state legislation designed to assure—at least in some circumstances—greater protection to interests that include but often are broader than those of incumbent management.[11]

CONTROL SHARE ACTS

The Ohio Control Share Acquisition Act is the most ambitious of the various second-generation laws enacted in the wake of *MITE*.[12] Whereas the first-generation statutes allowed state officials to delay and block hostile takeovers, the Ohio Act gives this power to target management and shareholders.[13] The Ohio legislators hoped that the law's reliance on the traditional corporate mechanism of shareholder approval would give the statute the immunity from Commerce Cause scrutiny enjoyed by state laws regulating internal corporate affairs.[14]

The central element of the Ohio Act and the statutes modeled after it is a provision requiring prior shareholder approval for tender offers and open market purchases deemed "control share acquisitions." These are defined as acquisitions that raise the acquiror's percentage ownership in the target company above specified thresholds. (The Ohio statute, for example, requires separate approval for purchases that result in the acquiror owning at least 20%, 33⅓%, or 51% of the target company's common stock; purchases by an acquiror who already owns 20% or more do not trigger the approval requirement unless the new purchases would raise the acquiror's ownership over the next threshold). The statutes forbid the consummation of control share acquisitions until approved by target company shareholders. Target management is required, within ten days after a prospective acquiror notifies the company, to call a special shareholders' meeting to vote on the proposed acquisition. The meeting must be held within 50 days of receipt of notice, and an affirmative vote of a majority of the disinterested shareholders is required.

11. 457 U.S. at 646–47.
12. Two other types of second-generation statute deserve mention: the so-called "fair price" statutes, which regulate second-step mergers (and similar transactions) undertaken by successful tender offerors after acquiring control of the target company, and Pennsylvania's Shareholder Protection Act. The fair price laws typically require the acquiror either to obtain approval for the second-step transaction by two supermajority votes, or to pay a "fair price" for the stock obtained in the second-step transaction. Maryland enacted the first, and most stringent, fair price statute (since copied by Connecticut, Kentucky, and Louisiana). The Maryland law requires second-step transactions to be approved by a vote of (a) 80% of all outstanding shares, and (b) two-thirds of all outstanding shares not held by the acquiror; or to meet certain "fair price" criteria, which in almost all circumstances yield a price substantially higher than the prices previously paid by the acquiror. Md. Corps. and Ass'ns Code Ann. §§3-601 et seq. Four other states (Michigan, Wisconsin, Georgia, and Virginia) have enacted less restrictive variations on the Maryland statute. See generally Hanks, *Maryland-Type Takeover Statutes: Are They "Fair Price" or Foul Ball?*, Nat'l L.J., Sept. 8, 1986 at 32, col. 3.
The constitutionality of the fair price laws has not yet been tested. Certain of the less restrictive fair price statutes (Michigan, Wisconsin, and Virginia) require only that the price paid in the second-step transaction be *equal* to the highest price previously paid. These statutes may be upheld as legitimate regulations of internal corporate affairs, since they prevent only second-step mergers that freeze out minority shareholders at an arguably unfairly low price. However, the fair price laws that require a ***higher*** price in the second step of the acquisition cannot be defended as a means of protecting minority shareholders. These laws appear designed to inhibit *all* two-step takeovers—an objective which, if Judge Posner's reasoning in *Dynamics* is followed (see infra, text accompanying notes 23–27), is impermissible under both the Commerce Clause and the Supremacy Clause. Pennsylvania's Shareholder Protection Act, Pa. Bus. Laws §§ 1408, 1409.1, 1910, takes a different approach. The law requires persons acquiring 30% or more of the voting power of a Pennsylvania corporation to pay the remaining shareholders (at their election) the "fair value" of their shares (determined as of the day before the acquisition of 30% ownership). It also requires that second-step mergers be approved by a vote of a majority of the disinterested shares, unless the merger is approved by a majority of the disinterested directors or is for a "fair price" (equal to the highest price previously paid). Finally, the statute provides that directors and officers, in discharging their duties, may consider "the effects of any action upon employees, suppliers and customers of the corporation, communities in which offices or other establishments of the corporation are located and all other pertinent factors."
Two of the Pennsylvania law's provisions—the forced buy-out provision for 30% shareholders and the majority voting rule for second-step mergers—may be vulnerable to constitutional attack on the same ground as the Maryland law: that their primary purpose and effect is to obstruct hostile acquisitions. The statute's other provision—apparently designed to relax the traditional rule that shareholders' interests take primacy over those of other corporate "constituencies"—may be protected by the internal affairs doctrine (see infra, text accompanying notes 20, 27, 34).
13. Ohio Rev. Code §§ 1701.01, 1701.831. The Ohio Act is applicable to acquisitions of shares of Ohio corporations with their principal place of business, principal executive offices, or substantial assets within Ohio. Ohio Rev. Code § 1701.01(Y).
14. Ohio Rev. Code §1701.832, which consists entirely of "findings" by the Ohio General Assembly in support of Ohio's takeover law, states that "responsibility for general corporate laws is the function of state legislation," and notes that the effect of the Ohio law will be to subject tender offers to "the normal corporate approval mechanisms involved in other typical types of acquisition transactions such as mergers, consolidations, combinations and majority share acquisitions."

The constitutionality of the control share acquisition statutes suffered a blow in the summer of 1985, when federal district courts invalidated Missouri's and Minnesota's control share acquisition statutes.[15] Additional blows, probably fatal, were delivered in the summer of 1986. Another federal district court struck down Hawaii's control share acquisition law[16]; the Sixth Circuit held Ohio's Control Share Acquisition Act invalid in *Fleet Aerospace Corp.* v. *Holderman*[17]; and in *Dynamics Corp.* v. *CTS Corp.*,[18] the Seventh Circuit invalidated the less restrictive control share acquisition law enacted by Indiana in an attempt to avoid constitutional objections to the Ohio Act.

Each of the five courts invalidated the control share acquisition statute before it under the Commerce Clause, as an excessive indirect burden on interstate commerce. In addition, three of the courts struck down the statute as a direct regulation of interstate commerce, and three of the courts held the statute invalid under the Supremacy Clause as well. While the analyses of all five courts are similar, the district court's opinion in *Fleet Aerospace* (which the Sixth Circuit largely adopted) provides the most extensive analysis of the constitutionality of the control share acquisition acts.

FLEET AEROSPACE

Fleet arose out of a tender offer by Fleet Aerospace, a Canadian company, for Aeronca, an Ohio corporation with its principal place of business and approximately 15% of its shareholders (but less than 5% of its shares) located in Ohio. Fleet sought declaratory and injunctive relief to bar enforcement of the Ohio takeover law. The district court issued a preliminary injunction, and the Sixth Circuit affirmed "for essentially the reasons stated by the district court."[19]

The district court held that the Ohio Act violated both the Supremacy Clause and the Commerce Clause. With respect to the Supremacy Clause, the court followed Justice White's plurality opinion in *MITE*, and held that the Williams Act embodies an affirmative congressional intention to favor neither incumbent management nor takeover bidders, and to preserve investor autonomy. The Ohio Act, the court held, undermines both neutrality and investor autonomy. By requiring shareholder approval of proposed acquisitions, the Act compels offerors to mount a proxy contest—with its additional costs and uncertainties—as well as a tender offer.

The Act further tips the balance in favor of management, the court held, by allowing the target board to delay the shareholder vote on a proposed offer until 50 days after the offer's commencement—long after the expiration of the 20-business-day waiting period mandated by the Williams Act. In fact, the court noted, management may be able to delay consummation of the offer longer still—perhaps even until after the expiration of the Williams Act's 60-day withdrawal period—by adjourning or challenging the shareholder vote, or by similar procedural tactics. Finally, the Act's shareholder approval requirement frustrates investor autonomy by allowing majority shareholders to block offers for less than a majority of the target company's stock.

The district court also held that the Ohio statute violates the Commerce Clause, both as a direct and as an indirect regulation of interstate commerce. The Act directly regulates interstate commerce, the court held, because (like the statute invalidated in *MITE*) it would apply even if neither the offeror nor a single one of the target company's shareholders were from Ohio. In addition, the Act imposes excessive burdens on interstate commerce in relation to the local interests it serves. By potentially blocking a nationwide tender offer, the Act prevents the target's shareholders (the great majority of whom are likely to be from out of state) from selling their shares at a premium, and also frustrates the other purposes served by the market for corporate control—providing an incentive to incumbent management to perform well (so as to avert a takeover), and reallocating economic resources to their highest valued use.

The court rejected the argument that the Act was a valid regulation of the internal affairs of Ohio corporations, akin to state laws requiring shareholder approval of mergers. Mergers and tender offers are fundamentally different, the court noted:

> A merger or other type of voluntary reorganization necessarily involves a basic change in the internal structure of a corporation. A tender offer does not . . . ; instead it involves transactions between an interested purchaser and individual shareholders who may or may not desire to sell the respective shares of stock they own.[20]

The internal affairs doctrine, the court held, protects state regulation of mergers and other corporate reorganizations, and may even protect state laws that incidentally affect

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15. *Icahn* v. *Blunt*, 612 F. Supp. 1400 (W.D. Mo. 1985); *APL Ltd. Partnership* v. *Van Dusen Air, Inc.*, 622 F. Supp. 1216 (D. Minn. 1985).
16. *Terry* v. *Yamashita*, CCH ¶ 92,845 (D. Hawaii 1986); *Gelco Corp.* v. *Coniston Partners*, _ F. Supp. _ (D. Minn. November 10, 1986).
17. 796 F.2d 135 (6th Cir. 1986).
18. 794 F.2d 250 (7th Cir. 1986), prob. juris. noted, 55 U.S.L.W. 3231 (Oct. 7, 1986).
19. *Fleet*, 796 F.2d 135, 139 (6th Cir. 1986), aff'g, 637 F. Supp. 742 (S.D. Ohio 1986). The Sixth Circuit only disagreed with the district court's conclusion "that *MITE Corp.* sounded the death knell for state control of federally regulated tender-offers, if the court meant by this statement that all state regulation regarding tender offers is foreclosed." 796 F.2d at 139 n. 5.
20. *Fleet*, 637 F. Supp. at 762.

tender offers, such as laws restricting the power of successful tender offerors to merge or otherwise reorganize the target corporation. But the internal affairs doctrine does not protect state laws that regulate tender offers directly.

Finally, the court dismissed Ohio's purported interest in preventing plant closings and layoffs caused by hostile takeovers. The claim that hostile takeovers harm Ohio's economy is speculative and unsupported by any evidence in the record, the court found. Moreover, even if takeovers did cause assets and employment to be transferred out of state, this would not justify state regulation:

> [A]ny legislative attempt by Ohio to control or restrict the ownership of stock of a corporation by regulating the interstate sale of that stock in order to prevent a new owner from closing an Ohio plant or transferring assets elsewhere would clearly be an unconstitutional interference with interstate commerce.[21]

DYNAMICS CORP.

The Seventh Circuit's decision in *Dynamics Corp.* v. *CTS Corp.*, striking down Indiana's takeover law, dealt an even greater blow to the constitutionality of the control share acquisition laws, and cast serious doubt on the constitutionality of *any* state legislation that significantly inhibits takeovers.[22]

Indiana's control share acquisition statute—enacted in 1986, after the initial cases invalidating control share acquisition laws—was designed to skirt the principal constitutional objections to the Ohio Act. Instead of allowing shareholders to *block* "control share acquisitions," the Indiana statute merely allows shareholders to penalize such acquisitions: it provides that no stock acquired in a "control share acquisition" shall have voting rights, unless the shareholders vote to grant the acquiror voting rights.[23] (Like the Ohio statute, the Indiana Act requires shareholders to vote within 50 days after the offeror notifies the corporation of the proposed acquisition.)

The careful drafting of the Indiana statute gave little pause to the Seventh Circuit, however, in *Dynamics Corp.* In a strongly worded opinion by Judge Posner, the Seventh Circuit affirmed the district court's invalidation of the Indiana statute on both preemption and Commerce Clause grounds. Judge Posner acknowledged that the statute was "[c]leverly drafted" but concluded that "the cleverness is fairly transparent." By imposing a heavy penalty (the loss of voting rights) on unapproved control share acquisitions, the Indiana law thwarts hostile takeovers almost as effectively as statutes that forbid unapproved acquisitions altogether:

> The offeror dare not accept the tendered shares till the stockholders' meeting is held, since if he loses the vote on voting rights he will end up with non-voting shares and will not be able to control the corporation—the main purpose of most tender offers. So he must hold the tender offer open for 50 days, rather than the 28 days required (on average) by the SEC's regulations under the Williams Act. See 17 C.F.R. §250.14e-1(a) (20 business days). And he can have no great confidence in being able to win the vote on voting rights, since he cannot vote his own shares.[24]

The delay and uncertainty imposed by the Indiana law, the Seventh Circuit found, constitute a "lethal dose" that few tender offers could withstand. By enabling target management and shareholders to block a nationwide tender offer, the Indiana law frustrates the purposes of the Williams Act and excessively burdens interstate commerce.[25]

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21. *Fleet*, 637 F. Supp. at 764.
22. It has been suggested that state statutes governing stock acquisitions in certain regulated industries, such as banking or insurance, are more likely than other takeover statutes to withstand constitutional scrutiny. In two cases, statutes governing insurance companies have been upheld on the basis of the McCarran-Ferguson Act, which provides that no congressional statute except one specifically relating to insurance shall supersede any state insurance law. See *John Alden Life Insurance Co.* v. *Woods*, CCH ¶ 98,617 (D. Idaho 1981) (court refused to preliminarily enjoin Idaho Acquisitions of Control and Insurance Holding Companies Systems Act, upholding Act under both Supremacy Clause and Commerce Clause); *Professional Investors Life Ins. Co.* v. *Roussel*, 528 F. Supp. 391 (D. Kan. 1981) (Kansas Insurance Holding Company Act constitutional under both Supremacy Clause and Commerce Clause). However, other decisions have invalidated similar statutes. See *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) (provisions of Missouri Insurance Holding Companies Act requiring prenotification and administrative hearings held unconstitutional under Supremacy Clause and Commerce Clause; McCarran-Ferguson Act not violated because statute regulates securities, not merely insurance); *Gunter* v. *AGO International, B.V.*, 533 F. Supp. 86 (N.D. Fla. 1981) (takeover provisions of Florida Insurance Holding Company Act held unconstitutional under Supremacy Clause; court did not consider McCarran-Ferguson Act). It is far from clear that such statutes would survive after *MITE*.
    In addition, some states have enacted statutes that regulate takeovers with a potential to affect the state's environment or natural resources. These laws (which typically require tender offerors to file disclosure statements and authorize a state official to call hearings and to block certain acquisitions) are not likely to withstand constitutional scrutiny. See *Mesa Partners II* v. *Unocal Corp.*, 607 F. Supp. 624 (W.D. Okla. 1985) (Oklahoma Energy Resources Conservation Act held unconstitutional under Commerce Clause; court found that Act was intended to regulate takeovers, not just to protect state resources).
23. Ind. Code §§ 23-1-42-1 et seq. The Indiana statute's jurisdictional reach is narrower than Ohio's. The Indiana statute applies only to acquisitions of shares of Indiana corporations with 100 or more shareholders, *and* with (i) their principal place of business, principal office, or substantial assets located in Indiana; *and* (ii) more than 10,000 shareholders or ten percent of their shareholders resident in Indiana, or more than ten percent of their shares owned by Indiana residents. Ind. Code § 23-1-42-4.
24. *Dynamics*, 794 F.2d at 261.
25. On the preemption issue, Judge Posner expressed some doubts about Justice White's conclusion in *MITE* that Congress intended the Williams Act not merely to be neutral as between management and takeover offerors, but to forbid state regulation favoring management. He concluded, however, that he was bound by the plurality opinion. *Dynamics*, 794 F.2d at 262.

Like the district court in *Fleet,* the Seventh Circuit dismissed the statute's purported benefits to state residents, characterizing them as "trivial or even negative." The court stated:

> No evidence has been presented that a takeover by Dynamics might reduce the value of CTS or lead to a shift of assets or employment from Indiana—and if it did lead to such a shift, this might further condemn, rather than save, the statute. The commerce clause does not allow states to prevent corporations from moving assets and employees to other states.[26]

Finally, the Seventh Circuit rejected the argument that the Indiana statute is a legitimate regulation of internal corporate affairs. Judge Posner noted that Indiana presumably has "broad latitude" in regulating internal corporate matters such as board elections, "even when the consequence may be to make it harder to take over an Indiana corporation." But, the court held, the internal affairs doctrine does not protect legislation such as Indiana's, which is plainly designed to inhibit hostile takeovers:

> [I]n this case the effect on the interstate market in securities and corporate control is direct, intended, and substantial; it is not merely the incidental effect of a general regulation of internal corporate governance. The law in question is an explicit regulation of tender offers; that the mode of regulation involves jiggering with voting rights cannot take it outside the scope of judicial review under the commerce clause. Any other conclusion would invite facile evasions of the clause.[27]

NEW YORK'S NEW TAKEOVER STATUTE

In December 1985, the New York State legislature enacted a new takeover statute,[28] designed to avoid the constitutional infirmities not only of the first-generation statutes but of the control share acquisition acts as well. Unlike the latter statutes, the New York law does not permit target management or shareholders to block or delay takeover bids, or even to deprive hostile acquirors of voting rights. Instead, the New York law merely limits the ability of hostile acquirors to effect a merger or other business combination with the target company after acquiring control of the company.

The central provision of the New York law prohibits an acquiror of 20% or more of the voting shares of a "resident domestic corporation" from engaging in a "business combination" with the corporation for a period of five years, unless, prior to the stock acquisition, the target's board approves either the acquisition or the subsequent business combination.[29] In addition, absent such prior approval, the acquiror is barred from engaging in a business combination with the target even after the five-year period elapses, unless the business combination either meets certain "fair price" requirements or is approved by the target's disinterested shareholders.[30]

The statute's jurisdictional reach is narrow, applying only to New York corporations with their principal executive offices *and* significant business operations in New York, *and* 10% of their voting stock beneficially owned by New York residents.[31]

The statute defines "business combination" very broadly, to include not only mergers or consolidations with the 20% shareholder or its affiliates, but a variety of other transactions as well. The definition includes any sale, transfer, or other disposition to the interested shareholder or its affiliates of assets of the corporation having a market value exceeding 10% of the corporation's total assets, outstanding stock, earning power, or net income. The definition also includes the issuance or transfer of 5% or more of the corporation's stock to the interested shareholder; plans for liquidation or dissolution; discriminatory transactions with the interested shareholder such as reclassification of securities or recapitalization; and any loans, pledges, or transfer of tax advantages by the corporation to the interested shareholder.[32]

In a memorandum submitted in support of the legislation, the office of the counsel to the governor stated that the bill is a response to the recent sharp growth in highly leveraged takeovers, which frequently result in a total or partial liquidation of the target. Such takeovers, the memorandum stated, adversely affect employees and communities; and the threat of such takeovers compels corporations to seek short-term profitability at the cost of long-term returns. According to the governor's memorandum, the New York law will discourage highly-leveraged hostile takeovers, by "making

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26. *Dynamics*, 794 F.2d at 264.
27. *Dynamics*, 794 F.2d at 264.
28. N.Y. Bus. Corp. Law § 912. The New York State Legislature also amended New York's Security Takeover Disclosure Act (discussed infra, at text accompanying notes 36–41), and enacted a new statute, N.Y. Bus. Corp. Law § 513(e), designed to prohibit "greenmail." Section 513(e) bars any "resident domestic corporation" from purchasing more than ten percent of its own stock from a shareholder for more than market value, unless the purchase is approved by both the board of directors and the shareholders. For a useful discussion of all of New York's new takeover provisions, see Sussman & Sussman, *Anti-Takeover Law Set For Litigation*, Legal Times, Jan. 20, 1986 at 1.
29. The board is required to approve or disapprove proposed acquisitions within 30 days after receipt of a good faith proposal from a prospective acquiror, or within "such shorter period, if any, as may be required by the [Securities] Exchange Act." N.Y. Bus. Corp. Law § 912(b).
30. N.Y. Bus. Corp. Law § 912(c) (3). These "fair price" provisions are designed to ensure that the price paid in the second-step transaction is equal to the highest price paid in the initial acquisition. Unlike Maryland's "fair price" statute (see n.12 supra), New York's fair price provisions do not require acquirors to pay a higher price in the second-step transaction than in the initial acquisition.
31. N.Y. Bus. Corp. Law § 912(a) (13).
32. N.Y. Bus. Corp. Law § 912(a) (5)

it more difficult, in the absence of prior board approval, for the takeover offeror to use the assets of the target to finance the takeover transaction."[33]

LIKELY EFFECTS

Despite the emphasis in the governor's memorandum on deterring highly leveraged takeovers, the New York law is likely to hinder many nonleveraged takeovers as well. The statute restricts the ability of successful tender offerors to effect a subsequent merger with the target, even though such second-step mergers are frequently used in nonleveraged acquisitions, as a convenient (and legitimate) means of eliminating minority shareholders.

Whether the statute's bar against second-step mergers will actually deter many takeover bids remains to be seen. The restriction does not seriously impede the efforts of successful tender offerors either to gain control of the target board or to operate the target company. And with acquirors daring to trigger poison pills, the restriction will probably soon be tested.

DOUBTFUL CONSTITUTIONALITY

The primary argument in support of the New York statute is that it does not regulate tender offers at all. The statute does not require any action or approvals before consummation of a tender offer; it merely restricts the offeror's power to effect a "business combination" with the target after the offer is completed. Thus, it can be argued, the New York law regulates internal corporate affairs, an area traditionally left to the states and immune from Commerce Clause scrutiny.[34] Moreover, the New York law regulates only post-tender offer transactions, which the Williams Act was not intended to regulate.

The force of this argument is substantially undercut by the Seventh Circuit's decision in *Dynamics.* The Indiana law invalidated there was similar to New York's statute in not allowing target management or shareholders to block or even delay hostile takeover attempts. The Indiana law penalized acquirors who failed to win shareholder approval (by depriving them of voting rights), but it did leave offerors free to complete their offers within the Williams Act timetable. The Seventh Circuit was not persuaded, however, that the Indiana statute was therefore constitutional. As Judge Posner noted, acquirors would be loathe to go forward with tender offers not knowing whether the shares they acquired would have voting power. Finding that the Indiana law was explicitly designed to frustrate hostile takeovers, the Seventh Circuit held that it was therefore not protected by the internal affairs doctrine, and was invalid under both the Commerce Clause and the Supremacy Clause.

If judged according to the principles set forth in *Dynamics Corp.,* the New York statute is likely to be found wanting. In its essential purpose and effect, the New York law is little different from the Indiana Act: both statutes are designed to strengthen management's hand in the face of hostile takeover attempts. The New York statute regulates takeovers less directly, and tips the balance less decisively in management's favor, than the Indiana statute. But, as the governor's memorandum in support of the New York law itself states, the law's basic objective is the same.

Without the protection of the internal affairs doctrine, the New York statute is likely to be invalidated under both the Supremacy Clause and the Commerce Clause. The New York statute enables target boards to hinder or block many (although not all) nationwide tender offers—including offers by bidders who plan to effect a second-step merger or liquidation, and perhaps also offers by bidders who plan to sell off most of the target company's assets. Such a result frustrates the objectives of the Williams Act (neutrality and investor autonomy) and excessively burdens interstate commerce.

A proponent of the New York statute might respond that the law burdens interstate commerce less and benefits state residents more than the Ohio and Indiana statutes, since the New York law is aimed at highly leveraged takeovers in particular rather than all hostile takeovers. However, even if this characterization of the New York law were correct, this would not be enough. The statute's benefits to New York residents would still be speculative, since it is doubtful that even highly leveraged takeovers of New York-based companies often result in the closing of New York plants and the transfer of assets and employment to other states. More important, as the courts in both *Dynamics* and *Fleet* held, any attempt by a state to prevent corporations from moving assets or employment to other states would be an unconstitutional interference with interstate commerce.[35]

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33. Governor's Program Bill Memorandum for 1985 Extraordinary Session at 6–9.

34. This argument derives some support from dicta in several of the control share acquisition cases. For example, in *APL Limited Partnership* v. *Van Dusen Air, Inc.*, 622 F. Supp. 1216 (D. Minn. 1985), a 1985 District of Minnesota decision invalidating Minnesota's control share acquisition act on Commerce Clause grounds, the court stated:
The acquisition of shares [in a tender offer] does not implicate the internal affairs of the target corporation. The use of that power *once the shares have been acquired* may well be a proper subject of state regulation. . . . 622 F. Supp. at 1223–24 (emphasis in original).

35. *Dynamics*, 794 F.2d at 264; *Fleet*, 637 F. Supp. at 764. *Cf. Lewis* v. *BT Investment Managers, Inc.*, 447 U.S. 27, 36 (1980). "However important the state interest at hand, it may not be accomplished by discriminating against articles of commerce coming from outside the State unless there is some reason, apart from their origin, to treat them differently' ".

NEW YORK'S DISCLOSURE LAW

New York's disclosure law, the New York Security Takeover Disclosure Act,[36] is much more likely to withstand constitutional scrutiny. This law (as amended in December 1985) is likely to serve as a model for other states' disclosure laws. It is carefully designed to provide local shareholders with information about a prospective takeover's likely impact on New York's economy, while avoiding constitutional pitfalls.

New York's disclosure law requires tender offerors to file a registration statement with the state attorney general (and deliver it to the target company) at the commencement of the offer.[37] Much of the information required in the registration statement—including information about the offeror's background and identity, source of funds, stockholdings, and purpose in making the acquisition—parallels Williams Act disclosure requirements. In addition, the New York law requires a statement as to the "potential impact" of the offeror's plans on New York residents, including any change in the location of the target's New York offices or business activities. Particulars about the bidder's labor relations and community activities must also be disclosed. (New York's Attorney General has discretionary power, however, to waive disclosure of any information that he determines to be "immaterial or otherwise unnecessary.")

The New York law authorizes the state attorney general to conduct investigations (but not hold public hearings) into the adequacy of disclosures. If he concludes that an offeror's disclosures are inadequate, he may bring a judicial action to enjoin the offer, and may also seek civil damages and criminal penalties. In addition, target shareholders residing in New York are given a private right of action for disclosure violations and are entitled to seek injunctive relief and damages.

Although the constitutionality of New York's disclosure law has not yet been tested, the law may well be upheld, particularly if the leading case on the constitutionality of state disclosure requirements, *Cardiff Acquisitions, Inc.* v. *Hatch,*[38] is followed.

In *Cardiff,* the Eighth Circuit upheld Minnesota's Corporate Takeovers Act—a disclosure law similar to, though perhaps less carefully drafted than, New York's—under both the Supremacy Clause and the Commerce Clause. Minnesota's law, like New York's, requires tender offerors to file a registration statement at the commencement of the offer, disclosing information relating to the proposed takeover's likely effect on state residents, as well as information required by the Williams Act. Unlike New York's law, the Minnesota law permits a state official (the Commerce Commissioner) to suspend a tender offer and hold a hearing on the adequacy of its disclosures. The Commissioner must reach a final decision within 19 days after the offer's commencement. If he concludes that the disclosures are inadequate, he may suspend the offer permanently, subject to the offeror's right to cure the disclosure deficiencies.

The Eighth Circuit in *Cardiff* held that the Minnesota Act is valid under the Commerce Clause, because it protects local investors and is not unduly burdensome to interstate commerce. The court noted that the Act's hearing provisions (unlike the hearing provisions struck down in *MITE*) are not likely to delay tender offers, since the Act requires the Commissioner to conclude hearings and render a final decision within 19 days after an offer's commencement—before the offeror is permitted under federal law to consummate the offer, and even before shareholders are permitted to withdraw tendered shares.[39]

The court also noted that the Act's disclosure requirements are useful and not excessive. By requiring disclosure parallel to that for the Williams Act, the law imposes little burden on offerors, while protecting local investors by permitting simultaneous state and federal enforcement (particularly useful, the court noted, in light of the SEC's strained resources). The additional disclosure requirements, relating to the offer's potential impact on Minnesota and its residents, also aid local investors, who may wish to consider this factor in deciding whether or not to sell their stock.[40]

The Eighth Circuit upheld most of the Minnesota Act's provisions under the Supremacy Clause as well, on the ground that the Act serves legitimate local interests and is "substantially consistent" with the Williams Act. Review by the Commissioner of an offeror's disclosures does not inter-

36. N.Y. Bus. Corp. Law §§ 1600–1613.
37. The disclosure law applies to any tender offer to purchase equity securities of a "target company" from a New York resident, if after the tender offer the offeror would own more than five percent of any class of the target company's equity securities. A "target company" is defined as a New York corporation that has either its principal executive offices or significant business operations in New York. N.Y. Bus. Corp. Law § 1601(a), (d).
38. 751 F.2d 906 (8th Cir. 1984).
39. Although the Minnesota Act authorizes the Commissioner to "prescribe different time limits than those specified" in the statute, the court noted that the Commissioner had not in fact extended the time limits. In addition, on the one prior occasion when the Act was enforced, the Commissioner actually offered to advance the hearing date rather than postpone it. "In light of this experience," the court concluded, "we have no reason to believe that the Minnesota Act will be applied in a manner which creates burdensome delay." *Cardiff,* 751 F.2d at 910–11.
40. The court also noted the Minnesota Act's narrow jurisdictional reach. The Act applies only to tender offers for stock of a corporation that has "substantial assets" in Minnesota and at least 20% of its equity securities beneficially held by Minnesota residents; in addition, any suspension of a tender offer applies only to Minnesota residents. See *Cardiff,* 751 F.2d at 911.

fere with the Williams Act's objectives, the court held, so long as the Commissioner does not judge the "quality" of the facts disclosed, require "evaluative, judgmental, or overly burdensome or irrelevant disclosures," or pass on the fairness of the offer. The court accordingly upheld most of the Act's disclosure requirements, but invalidated two provisions requiring offerors to disclose such "additional information [as] the commissioner may by rule prescribe." These provisions, the court held, "are unconstitutionally vague and may require the disclosure of irrelevant or confusing data and may require judgmental data that the Commissioner has no authority to require."[41]

CONCLUSION

The Supreme Court's decision in *Dynamics* will undoubtedly provide greater clarity in this area, while at the same time spawning a new generation of state statutes designed to squeeze through the interstices of the Court's opinion. For the moment, however, the disclosure provisions of New York's takeover law may well withstand constitutional scrutiny, because they serve legitimate state interests without impeding the interstate market for corporate control. By contrast, the substantive provisions of New York's takeover law serve state interests only by sheltering New York companies from the corporate control market. Protectionism of this sort is not likely to survive judicial review, at least if the principles expressed in *Fleet* and *Dynamics* are followed.■

41. 751 F.2d at 914.