

2014

The Power to Decide on Takeovers: Directors or Shareholders, What Difference Does it Make?

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Matteo Gatti, *The Power to Decide on Takeovers: Directors or Shareholders, What Difference Does it Make?*, 20 Fordham J. Corp. & Fin. L. 73 (2014).

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The Power to Decide on Takeovers: Directors or Shareholders, What Difference Does it Make?

Cover Page Footnote

Assistant Professor of Law, Rutgers School of Law – Newark. I wish to thank Lucian Bebchuk, John Coates, Luca Enriques, James Fanto, Martin Gelter, Minor Myers, Chrystin Ondersma, Mark Roe, Eric Pan, Arthur Pinto, Fadi Shaheen, Matteo Tonello, Bill Wang and various members of Faculty at Rutgers School of Law – Newark for commenting on, proving feedback or supporting, this article (in present or earlier form). A special thanks to John Laide and FactSet SharkRepellent for tremendous data support. Invaluable research help by Jennifer Amarnath and Rob Hayes is acknowledged. All errors and omissions are my own

THE POWER TO DECIDE ON TAKEOVERS: DIRECTORS OR SHAREHOLDERS, WHAT DIFFERENCE DOES IT MAKE?

*Matteo Gatti**

ABSTRACT

This Article analyzes the allocation of the power to decide on hostile takeovers as between directors and shareholders. In it I show who actually has power in a takeover and what factors are at work to grant that authority. Although directors are traditionally considered to be in charge of deciding the outcome of a hostile takeover of a Delaware corporation, shareholders nevertheless may have the power to reverse the outcome through a vote. Even though shareholders sometimes lack the power to determine the outcome of a takeover bid, the reason for that is not embedded in the takeover regime itself. Instead, rules, principles, and practices of corporate law that are external to the takeover regime act as barriers to shareholder power. These barriers, which I designate “corporate law collateral factors,” include staggered boards, limitations to director removability, the inability of shareholders either to call special meetings or to act by written consent, supermajority rules, proxy regimes, and conflict of interest regimes. This Article reports original empirical evidence on the number and market capitalization of Delaware companies that are affected by each corporate law collateral factor and argues that scholars and courts have overemphasized the importance of the takeover regime itself and underemphasized the corporate law collateral factors. Policymakers and interpreters should thus address all corporate law collateral factors within the body of takeover law, whether or not statutory. Given the importance of takeovers, it is strange not to consider them in the context of tailored rules that acknowledge the existence and

* Assistant Professor of Law, Rutgers School of Law – Newark. I wish to thank Lucian Bebchuk, John Coates, Luca Enriques, James Fanto, Martin Gelter, Minor Myers, Chrystin Ondersma, Mark Roe, Eric Pan, Arthur Pinto, Fadi Shaheen, Matteo Tonello, Bill Wang and various members of Faculty at Rutgers School of Law – Newark for commenting on, proving feedback or supporting, this article (in present or earlier form). A special thanks to John Laide and FactSet SharkRepellent for tremendous data support. Invaluable research help by Jennifer Amarnath and Rob Hayes is acknowledged. All errors and omissions are my own.

impact of such factors. Leaving the corporate law collateral factors in a vacuum to general corporate law does a disservice to takeover players and stakeholders.

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INTRODUCTION

This Article analyzes the allocation of power between directors and shareholders in hostile takeovers. It explores who actually has power in a hostile takeover and what factors are at work to bestow such power. Although directors are traditionally considered to be in charge in deciding the outcome of a hostile takeover of a Delaware corporation, shareholders nevertheless may have the power to reverse the outcome via a vote.¹ This Article argues that even though shareholders often lack the power to determine the outcome of a takeover bid, the reason for that is not embedded in the takeover regime itself. Instead, combinations of rules, principles, and practices of corporate law that are external to the takeover regime act as barriers to shareholder power.

Let us start with takeover laws. The regulation of anti-takeover defenses is arguably one of the most debated topics in corporate law. Common wisdom suggests that there are few other fields in corporate governance with so little convergence in the most developed financial markets. During the 1980s, state legislatures and courts in the United States responded to an unprecedented surge in hostile takeovers by providing companies the freedom to adopt defenses in response to unsolicited bids.² Delaware in particular made it clear that, so long as shareholders can replace a board through a proxy fight when faced with an unsolicited tender offer, directors have the power to keep the

1. See *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 959 (Del. 1985).

2. See Mark J. Roe, *Takeover Politics*, in *THE DEAL DECADE: WHAT TAKEOVERS AND LEVERAGED BUYOUTS MEAN FOR CORPORATE GOVERNANCE* 321, 340-47 (Margaret M. Blair ed., 1993) [hereinafter Roe, *Takeover Politics*] (lobbying efforts by corporations resulted in the enactment of various anti-takeover laws throughout the United States, with Delaware adopting a mild approach to avoid the risk of federal intervention).

company independent and therefore erect (or maintain existing) anti-takeover devices, most notably, the poison pill.³

The law evolved quite differently in Europe, where two opposite regimes emerged. Since the late 1950s, target companies in the United Kingdom have been subject to some variation of the “board neutrality rule,” which prohibits the board of a target company from engaging in defensive actions without shareholder approval.⁴ In contrast, long-standing aversion to takeover-capitalism in countries like Germany and the Netherlands allowed companies to use defenses. These differing approaches led to a compromise on the European Union’s 2004 Directive on Takeover Bids (the “Directive”), which made optional the regulation of takeover defenses. The Directive adhered to the board neutrality rule,⁵ but it allowed each Member State to decide whether to implement it; however, if a Member State rejected the rule, companies incorporated in that State could still implement it on a voluntary basis.⁶

3. See *Moran v. Household Int’l, Inc.*, 500 A.2d 1345, 1351, 1353 (Del. 1985) (adopting a rights plan by the board of directors of a target as a prospective takeover defense is protected by the business judgment rule).

4. See John Armour, Jack B. Jacobs & Curtis J. Milhaupt, *The Evolution of Hostile Takeover Regimes in Developed and Emerging Markets: An Analytical Framework*, 52 HARV. INT’L L.J. 219, 235-36 (2011) (noting that the principle was first encapsulated in the Notes on Amalgamation of British Businesses in the autumn of 1959, which was self-regulation adopted by “a committee consisting of trade groups representing merchant banks, institutional investors, the largest commercial banks, and the London Stock Exchange,” which had been secretly invited by the Governor of the Bank of England to craft takeover rules in the aftermath of the takeover of British Aluminium of 1958) for a discussion of the origins of the board neutrality rule.

5. Under the board neutrality rule, the directors of a target company are compelled to obtain prior shareholders’ authorization when engaging in defensive actions, “which may result in the frustration of the bid.” Directive 2004/25/EC, of the European Parliament and of the Council of 21 April 2004 on Takeover Bids, 2004 O.J. (L 142) 19.

6. Council Directive 2004/25, art. 12, 2004 O.J. (L 142) 21 (EC); see also *Commission of the European Communities, Commission Staff Working Document: Report on the Implementation of the Directive on Takeover Bids*, at 3-5, SEC (2007) 268 (Feb. 21, 2007) [hereinafter *Report on the Implementation of the Directive on Takeover Bids*]. The European Legislature also introduced a reciprocity mechanism under which Member States can decide whether to relax the prohibitions and restrictions arising out of the board neutrality rule in the event a bid is made by a company not subject to such rules. Council Directive 2004/25, art. 12, 2004 O.J. (L 142) 21 (EC). Therefore, the Directive is optional in what is arguably one of its most significant rules. Matteo Gatti, *Optionality Arrangements and Reciprocity in the European Takeover Directive*, 6 EUR. BUS. ORG. L. REV. 553, 558-59 (2005) (showing

Subsequently, while the United Kingdom and (at least initially) France enacted the board neutrality rule, Germany did not.

This Article analyzes the different allocation of corporate powers between directors and shareholders when responding to an unsolicited acquisition in the Delaware system, a pro-target regime, as opposed to jurisdictions like the U.K. system or other pro-shareholder regimes that have adopted the board neutrality rule. In particular, the purpose of this Article is to provide a structural assessment of the ultimate differences between the two approaches.

Traditionally considered antithetical by legal commentators,⁷ the Delaware and U.K. systems are in fact similar in that *in both, a shareholder vote can play a pivotal role in the outcome* of an unsolicited acquisition attempt.⁸ For example, Delaware allows companies to adopt and maintain defenses subject to the possibility for the bidder to oust the board through a shareholder vote.⁹ In contrast, the U.K. system prohibits

that national legislatures can choose among sixteen different regimes, with the possibility for companies to opt-in to the board neutrality rule even if their Member State did not adopt it). For a while, the regimes adopted in the three biggest markets—the United Kingdom, France, and Germany—were different from one another. *Report on the Implementation of the Directive on Takeover Bids*, at 12 (showing that (i) the United Kingdom adopted the board neutrality rule and not the reciprocity option, (ii) France had adopted both the board neutrality rule and the reciprocity option, and (iii) Germany did not adopt the board neutrality rule, but it did adopt the reciprocity option). In 2014, France reformed its takeover law and converted the board neutrality rule into an opt-in provision: see Article 10(V) of Loi 2014-384 of March 29, 2014 “visant à reconquérir l’économie réelle” (literally “aiming to reconquer the real economy”).

7. See, e.g., John Armour & David A. Skeel, Jr., *Who Writes Takeover Regulation and Why: The Peculiar Divergence of U.S. and U.K. Takeover Regulation*, 95 GEO. L.J. 1727, 1729 (2007) (stating that “unless shareholders consent, the [U.K.] Code strictly prohibits management from employing any defensive tactics that would have the effect of frustrating an actual or anticipated bid. In contrast, management in the United States has a good deal more flexibility to engage in defensive tactics, provided that these can be justified in accordance with their fiduciary duties”); see also Edward F. Greene, *Regulatory and Legislative Responses to Takeover Activity in the 1980s: The United States and Europe*, 69 TEX. L. REV. 1539, 1574 (1991) (noting that “the ability of directors in the U.K. and Europe to use takeover defenses is much more limited than that of their American counterparts” and that “[a]t one extreme is the U.K., where directors are very much accountable to shareholders”).

8. Lucian A. Bebchuk & Oliver Hart, *Takeover Bids Vs. Proxy Fights in Contests for Corporate Control* 4 (Harvard Law Sch., John M. Olin Ctr. Law, Econ. & Bus., Discussion Paper No. 336, 2001), available at <http://ssrn.com/abstract=290584>.

9. This Article does not focus on the fiduciary duties of directors under *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986). The *Revlon* ruling established an enhanced standard of conduct that compels directors to maximize

defenses unless shareholders expressly give their approval. Another way to look at the two systems is to consider them as if they set forth two different “default”¹⁰ regimes. The difference ultimately being the beneficiary of shareholder inertia: in other words, whom the regime favors if no shareholder vote occurs (targets in Delaware and bidders in the United Kingdom).

Integral to both regimes is that each “default” can be reversed by a shareholder vote. Since there is money on the table once a decision to go hostile is taken – and hence the right incentives for the parties involved¹¹

value for the benefit of shareholders in the sale of the company above the protection of interests of other stakeholders, including maintaining the independence of the corporate entity. Specifically, under *Revlon* the role of directors was transformed “from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company.” *Id.* at 182. *Revlon* duties are triggered in certain limited circumstances (e.g., if a company is put on sale—either in a stock or in an asset deal—or if a break-up is inevitable). This Article does not analyze *Revlon* because directors of a Delaware target company have, at least from a pure legal standpoint, the ability to resist (potentially on a protracted basis) a hostile bid to maintain independence without ever becoming subject to the *Revlon* duties. In other words, if directors fall under *Revlon*, it is because they choose so—although sometimes it is for lack of better defensive options that they regrettably end up selling to a white knight.

10. This Article deliberately uses the term “default” in non-technical fashion. By “default” the Article does not refer to the generally accepted corporate law meaning of a statutory rule that parties can contract around either in the certificate of incorporation or in the bylaws. Rather, the term “default” in this Article means a regime imposed by the legislature that generally cannot be opted out of in the corporation’s organizational documents, but that shareholders can depart from by adopting certain resolutions to reverse such a regime.

11. Traditionally, proxy fights in the context of hostile acquisitions have been considered different than proxy fights in general, in that in the former shareholders are said to have the right incentives to make a decision between the offer price and the expected long-term value of the shares: if the offer price is considered greater than the value of the company staying independent, they will vote for the insurgents, otherwise they will stick to the incumbents. Conversely, in plain vanilla proxy fights, shareholders generally do not have enough information about rival teams and usually end up erring in favor of incumbents. *See* Bebchuk & Hart, *supra* note 8, at 2 and 5 (noting that “voting works better when the choice is between the incumbent’s uncertain value and the certain value of an offer in cash or publicly traded securities, and less well when the choice is between the incumbent’s uncertain value and the rival’s uncertain value”); Lucian A. Bebchuk & Marcel Kahan, *A Framework for Analyzing Legal Policy Towards Proxy Contests*, 78 CAL. L. REV. 1071, 1101 (1990) (explaining that uncertainty in an insurgent’s quality is often a critical factor in helping incumbents win proxy contests). However, this distinction may be jeopardized by the contemporary rise in successful proxy fights waged by activist hedge funds where no tender offer is on the

to determine to reverse it – the decision to adopt one regime over the other does not necessarily have any significant impact on the final outcome. That is, ultimately, such differences in anti-takeover regime might not really matter.¹²

To be sure, to not actually matter, the regimes must be easily reversible. Indeed, I argue that, for the two regimes to be immaterial to the outcome of an acquisition, the degree of their reversibility is the most crucial aspect: if the parties that aim to change the legal status quo find that they are unduly burdened or that they do not have equal chances to prevail, setting the default one way or the other will have a tangible impact on the final outcome. This Article analyzes a series of factors that affect reversibility of the default including: (i) rules governing shareholder voting and director elections, and (ii) types of defenses that a target company's board can choose to fend off a bid.

Ultimately, both systems give shareholders some sort of control via a vote, yet they set a different starting point with the default. As long as there are no barriers to the vote or to the goals the vote purports to attain, that is, no barriers to reversing the default, both regimes leave control in the hands of shareholders. Thus, if shareholders do *not* have control in the end, it is not because of the default regime, but rather because factors external to the takeover regime acted as barriers to reversing the default. Hence, the *combination* of the default and these external factors is key in determining the final outcome (or in making a reversal so difficult *ex ante* that no private parties will bother taking steps to effect it). This has important implications. In particular, if we believe that a takeover regime gives too little or too much control over the outcome of an acquisition to shareholders, we need to look not at the initial allocation of power (the default), but at the barriers to making changes to the default.¹³

The Article is structured as follows: Part I describes the allocation of corporate powers between directors and shareholders in connection

table and insurgents actually manage to appoint their nominees. *See generally* David A. Katz & Laura A. McIntosh, *Corporate Governance Update: Heightened Activist Attacks on Boards of Directors*, N.Y. L.J. (July 24, 2014).

12. *See infra* note 86 for an assessment and contextualization of some recent European literature that proposes an approach similar to that applied throughout this Article.

13. In other words, it is the takeover regime's reversibility that matters—not the takeover regime itself. And therefore it is imperative to identify the combination of the regime with the actual barriers to reversing it.

with the defense of a target company in Delaware.¹⁴ In particular, the Article provides an overview of the evolution of Delaware corporate law starting with the proliferation of defenses in the 1980s, then looking at the anti-defense movement that shareholder activists introduced at the beginning of the 2000s, and finally assessing the current resurgence of defenses in the aftermath of the financial crisis and a new rise in acquisitions structured via tender offers. Part II analyzes what would be the consequences of a “pro-shareholder Delaware.” Part III.A argues that the two apparently antithetical regimes are ultimately not so different, since both give shareholders the final say in an acquisition. Part III.B identifies the reversibility of the regime and the ability to adopt so-called structural defenses as the crucial variables that make the difference. Both depend on certain rules, principles, or practices of corporate law that are external to the actual takeover regime (the Article labels them as “corporate law collateral factors,” which include shareholders’ ability to call special meetings or act by written consent, supermajority rules, proxy and conflict of interest regimes, staggered boards, and director removability). I note that the difference is not only between two default regimes, but also in the potential outcome of the acquisition, irrespective of the actual default regime. Part III.C reports original empirical evidence on the number and market capitalization of Delaware companies that have been affected by each corporate law collateral factor. Part IV assesses how, in light of the corporate law collateral factors, the two default regimes are capable of giving shareholders some power in determining the outcome of the acquisition. Part IV concludes.

14. Part I describes the evolution of the takeover regime in Delaware, while it does not dedicate a similar description to the evolution of the U.K. regime. British rules did not witness the great tension and controversy that corporate America experienced since the 1960s with respect to hostile takeovers. In the United Kingdom, the board neutrality rule and shareholder primacy in takeovers were endorsed in the late 1950s as a sound policy solution in the aftermath of the British Aluminium takeover of 1958 and were subsequently adopted in 1968 in the very first version of self-regulation in the United Kingdom, the City Code on Takeovers and Mergers. *See* Armour, Jacobs & Milhaupt, *supra* note 4, at 235-37.

**I. ALLOCATING THE POWERS BETWEEN DIRECTORS AND
SHAREHOLDERS IN THE DEFENSE OF DELAWARE TARGET COMPANIES**

**A. THE PROLIFERATION OF DEFENSES IN THE 1980S AND THE RISE OF THE
POISON PILL**

Both policy and positive law issues related to hostile takeovers have initially focused only on the takeover regime itself. This became especially apparent after courts in Delaware emphasized shareholders' alleged power to oust directors and therefore their alleged control on the ultimate outcome of takeover contests. This part of the article describes how Delaware law evolved in this respect.

Hostile takeovers have had a long-lasting impact on corporate America and the evolution of corporate law in the United States. The law of corporate acquisitions in the United States experienced a substantial development in the 1960s when Congress passed the Williams Act in 1968 as a response to a chain of hostile transactions known as Saturday Night Special raids.¹⁵ In such transactions purchasers used to seek control of companies through the following coercive technique: bidders would announce an offer to purchase approximately half of a company's stock right after the market close on Friday, the offer would be kept open over the weekend and shareholders would tender their shares on a first-come, first-serve basis—no federal disclosure requirements were mandated at the time so bidders could decide to limit the information to a minimum. The lack of time to decide, the lack of information, and the first-come, first-serve mechanism put enormous pressure on shareholders to accept the offer at whatever price, even if most of the time the deal they were getting was not attractive. The response from the federal legislature was limited, as it only required bidders to provide disclosure and make tender offers subject to some basic procedural rules to foster equality of treatment¹⁶

15. Securities Exchange Act of 1934, §§ 13(d)-(f), 14(d)-(f), *amended by* the Williams Act, Pub. L. No. 90-439, 82 Stat. 454 (1968) (codified as amended at 15 U.S.C. §§ 78(a) et seq. (2012)). See Ronald J. Gilson, *The Case Against Shark Repellent Amendments: Structural Limitations on the Enabling Concept*, 34 STAN. L. REV. 775, 775 n.2 (1982); Dale A. Oesterle, *The Rise and Fall of Street Sweep Takeovers*, 1989 DUKE L.J. 202, 217 (1989).

16. The most important being the requirement that corporations accept offers on a pro-rata basis. This functioned to avoid inequality that resulted from shareholders, in a typical common pool setting, racing against one another (and, in the end, their own interests) to tender shares before it is too late. Section 14(d)(6) of the Williams Act

and a minimum mandatory period¹⁷ for the offer to stay open in order to allow alternative bidders to enter the control contest and trigger auctions.¹⁸

Early in the 1980s, with the so-called two-tier, front-end loaded tender offers, corporate raiders and hostile bidders managed to overcome the light response with which the federal legislature was able to shut down the Saturday Night Special raids. Two-tier tender offers were structured with a partial offer at some premium over the market price in the front-end and a low-ball take-out merger in the back-end.¹⁹ In what some consider a typical prisoner's dilemma situation, shareholders were pressured to tender their shares because they feared that the bid would succeed and they would be stuck with shares to be taken out at a very low price in the second-step merger.²⁰

originally imposed the pro-rata requirement for shares tendered in the initial ten days of the offer; however, in 1982, the Securities and Exchange Commission ("SEC") promulgated Rule 14d-8, which extended proration to the entire offer period. *See* VICTOR BRUDNEY & WILLIAM W. BRATTON, *CASES AND MATERIALS ON CORPORATE FINANCE* 1010 (4th ed. 1995).

17. Prior to the SEC's 1979 enactment of Rule 14e-1, which expressly requires that offers be made for a minimum period of twenty working days, the Williams Act originally imposed a minimum of seven days for any-and-all offers and ten days for partial offers. These requirements were considered implicit under Section 14(d)(5) and Section 14(d)(6). 17 C.F.R. § 240.14d-5 (2012) (stating that shareholders may withdraw their tenders in the initial seven days of an offer); 17 C.F.R. § 240.14d-6 (pro-rata rule applies in the initial ten days of a partial offer). *See* RONALD J. GILSON & BERNARD S. BLACK, *THE LAW AND FINANCE OF CORPORATE ACQUISITIONS* 947 (1995).

18. *See* ROBERT C. CLARK, *CORPORATE LAW* 546-54 (1986).

19. *See* Martin Lipton & Paul K. Rowe, *Pills, Polls and Professors: A Reply to Professor Gilson*, 27 *DEL. J. CORP. L.* 1, 5 (2002) ("The goal of [front-end-loaded] bids was . . . to 'bust-up' the corporation and sell the pieces for a quick profit."); *see generally* William J. Carney, *Shareholder Coordination Costs, Shark Repellents, and Takeout Mergers: The Case Against Fiduciary Duties*, 1983 *AM. B. FOUND. RES. J.* 341, 373 (1983) (discussing how when faced with two-tier bids, corporations should be allowed to adopt shark repellents to help shareholders coordinate for a common response to a low ball offer); Victor Brudney & Marvin A. Chirelstein, *Fair Shares in Corporate Mergers and Takeovers*, 88 *HARV. L. REV.* 297, 298 (1974) (explaining that bidders have a fiduciary duty toward minority shareholders in second-step takeout mergers).

20. *See* Carney, *supra* note 19, at 348-49. In short, shareholders end up accepting an offer that is not in their best interest because they cannot coordinate and reject it, in the same way both prisoners end up confessing because they cannot agree on the story to tell. Absent coordination, actions taken by each shareholder in his or her self-interest lead to sub-optimal outcomes. *See* Ronald J. Gilson, *A Structural Approach to*

Companies reacted on two different fronts. On one hand, they (quite successfully) lobbied state legislatures to pass anti-takeover statutes;²¹ on the other hand, they “privately” responded to coercive offers with the adoption of a wide array of defensive tactics, including, most notably, shareholders’ rights plans — better known as poison pills.

The most common and effective version of shareholders’ rights plans, the flip-in plan, gives stockholders (other than a potential acquirer) rights to purchase stock at a considerable discount if a potential acquirer increased its stake in the target in excess of a certain threshold of beneficial ownership.²² The threshold normally ranges from

Corporations: The Case Against Defensive Tactics in Tender Offers, 33 STAN. L. REV. 819, 859-62 (1981) for a view critical of the common characterization of two-tier bids as raising prisoner’s dilemma concerns.

21. See Roberta Romano, *The Future of Hostile Takeovers: Legislation and Public Opinion*, 57 U. CIN. L. REV. 457, 458-65 (1988).

22. The threshold is generally calculated by incorporating by reference the “group” definition for beneficial ownership purposes under Rule 13(d)-3 of the Securities Exchange Act of 1934, which aggregates purchases made by different persons acting together as a group (“[w]hen two or more persons act as a . . . group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a ‘person’ for the purposes of this subsection”). See 17 C.F.R. § 240.13d-5(b)(1) (2011). For a description of how, in the current market environment, such a definition has proven incapable to aggregate purchases by hedge funds acting via wolf packs, see John C. Coffee Jr. & Darius Palia, *The Impact of Hedge Fund Activism: Evidence and Implications* 23, 33-36, (ECGI Law, Working Paper No. 266, 2014), available at <http://ssrn.com/abstract=2496518>. Professors Coffee and Palia mention that companies might consider adopting a poison pill that “could broadly define its coverage so as to apply to any persons ‘acting in concert’ or ‘in conscious parallelism’ with the leader of the ‘wolf pack;’” such a pill would require to “define ‘group’ for purpose of the poison pill much more broadly than the case law under the Williams Act.” *Id.* at 77. Market players, practitioners, and courts have also focused on derivative contracts, synthetic ownership, and so-called empty voting. See generally Henry T. C. Hu & Bernard Black, *The New Vote Buying: Empty Voting and Hidden (Morphable) Ownership*, 79 S. CAL. L. REV. 811 (2006). While the court’s decision in *CSX Corp. v. Children’s Investment Fund Management* applied the anti-fraud provision in Rule 13d-3(b) prohibiting arrangements with the purpose or effect of circumventing the beneficial ownership reporting rules to certain empty voting practices, it also gave derivative players some guidance on how to avoid tripping such anti-fraud provision; companies started to extend the definition of beneficial ownership to expressly cover practices including empty voting and derivatives. *CSX Corp. v. Children’s Inv. Fund Mgmt. (UK) LLP, et al.*, 562 F.Supp 2d 511 (S.D.N.Y. 2008), *aff’d in part, vacated in part, remanded*, 654 C.3d 276 (2d Cir. 2011); see also Charles M. Nathan & Stephen Amdur, *Second Generation Advance Notice Bylaws and Poison Pills*, HARV. L. SCH. F. ON GOVERNANCE & FIN. REG. (Apr. 2, 2009, 9:31 AM), <http://blogs.law.harvard.edu/corpgov/2009/04/22/second-generation-advance-notice-bylaws-and-poison-pills/>

5% to 20%.²³ Effectively, a plan threatens significant economic and voting dilution to a potential acquirer unless a target's board takes action to redeem the subscription rights.²⁴

The pill is particularly appealing for two reasons. First, it does not require any shareholder action for its adoption or redemption. Therefore, it is a useful device for directors seeking protection from hostile acquisitions.²⁵ Second, the pill really functions as a deterrent, a threat of dilution for an unsolicited acquirer, without the need for an actual transaction by a target company. The mere fact that the pill is in place compels a bidder to try either to negotiate a friendly deal with the board or to replace (or threaten to replace, if the threat would sound credible enough given the target's ownership structure) the board through a proxy contest to get rid of the pill. This calls for persuading enough

(discussing transparency and accountability for synthetic equity and empty voting in addition to second-generation poison pills).

23. Lucian A. Bebchuk & Robert J. Jackson, Jr., *The Law and Economics of Blockholder Disclosure*, 2 HARV. BUS. L. REV. 39, 56 (2012), mentioning that, based on a SharkRepellent dataset of early 2012, of the 805 public companies with a pill in place, seventy-six percent had a pill trigger at an ownership threshold of fifteen percent or less, and fifteen percent of such companies have pills triggered by a threshold of ten percent or less. The low-end of the range is a development in poison pill design that aims to protect a company's tax assets. See *infra* note 48 and accompanying text. Note that, more recently, companies have started distinguishing between passive and active investors for pill threshold purposes: in the Sotheby's case, the company adopted a pill with a 10% threshold for activist investors, and with a 20% threshold for passive ones—such a pill was considered valid by the Delaware Chancery Court in *Third Point LLC v. Ruprecht*, 2014 Del. Ch. LEXIS 64 (Del. Ch. May 2, 2014).

24. Typically, when a pill is triggered, each shareholder (other than the potential acquirer) has a right to receive, upon exercise, shares having a value—based on the then current market price—equal to two times the exercise price of the right. See, e.g., GILSON & BLACK, *supra* note 17, at 741-42 (providing a copy of a share purchase rights plan to exhibit the mechanics of the pill); see Jonathan R. Macey, *The Legality and Utility of the Shareholders Rights Bylaws*, 26 HOFSTRA L. REV. 835, 839-40 (1998); Jeffrey N. Gordon, *An American Perspective on Anti-takeover Laws in the EU: The German Example*, in REFORMING COMPANY LAW AND TAKEOVER LAW IN EUROPE 541, 549 (Guido Ferrarini et al. eds., 2004) (“[T]he flip-in pill operates through a discriminatory issuance of cheap shares that would massively dilute the hostile bidder's stake.”).

25. Marcel Kahan & Edward B. Rock, *How I Learned to Stop Worrying and Love the Pill: Adaptive Responses to Takeover Law*, 69 U. CHI. L. REV. 871, 909-10 (2002). However, this does not mean that shareholders are completely prevented from having a say on poison pills.

shareholders and gives those shareholders ultimate control over the outcome.²⁶

To be sure, since the mid-1980s bidders have also turned to litigation to challenge the validity of the pill, but that strategy did not prove successful notwithstanding the majority of legal and financial scholars opposed to defensive measures.²⁷ When the legality of takeover

26. John C. Coates IV, *Ownership, Takeovers and EU Law: How Contestable Should EU Corporations Be?*, in REFORMING COMPANY LAW AND TAKEOVER LAW IN EUROPE 677, 681 n.18 (Guido Ferrarini et al. eds., 2004); see also Jordan M. Barry & John William Hatfield, *Pills and Partisans: Understanding Takeover Defenses*, 160 U. PA. L. REV. 633, 643-44 (2012). Bidders do not necessarily have to mount a proxy fight every time they go hostile, as the proxy fight can operate “in the shadow.” If the ownership structure of the given target is such that its directors can anticipate they would be losing in a proxy fight, it is not uncommon that they would let the acquisition go through if a bidder is credible in threatening to be ready to start a proxy fight and replace the board. This is what happened in a couple of deals in 2012. For example, in GlaxoSmithKline’s acquisition of Human Genome Sciences, a deal valued at approximately \$2.84 billion, the target agreed to be acquired by the bidder for \$14.25 per share (a hostile tender offer at \$13 had been launched a few months before). The bidder made it clear it might solicit shareholder consents to replace the board if the target did not accept the offer. See Mark Scott, *Glaxo Said to Aim to Replace Human Genome’s Board*, DEALBOOK (May 31, 2012, 9:54 AM), <http://dealbook.nytimes.com/2012/05/31/glaxo-said-to-be-looking-to-replace-human-genomes-board/> (last visited Dec. 3, 2014). Similarly, in Cypress Semiconductor’s acquisition of Ramtron International, a deal valued at approximately \$110 million, after the bidder increased its hostile tender offer from \$2.68 to \$2.88 per share, the target ultimately agreed to be acquired at \$3.10 per share, following the bidder’s threat to solicit written consents to replace the board if the target continued to reject the offer. See E-mail from T.J. Rodgers, President and CEO, Cypress Semiconductor Corp., to Ramtron Int’l Corp. Board of Directors (Aug. 6, 2012), available at <http://www.cypress.com/?rID=67318> (“If the board and management continue to entrench themselves and destroy stockholder value through continued poor performance and an undefined strategic process, we may be forced to seek out new directors who are more committed to maximizing value for your stockholders.”); see also Ramtron Int’l Corp., Proxy Statement (Schedule 14A), at 26 (Aug. 27, 2012), available at <http://www.sec.gov/Archives/edgar/data/791915/000119312512368926/d368389ddf14a.htm>. My claim is in line with the empirical literature finding that companies and CEOs would rather let go or significantly amend certain deals than facing the risk of a defeat at a shareholder meeting: see Mario Becht et al., *Does Mandatory Shareholder Voting Prevent Bad Acquisitions?* 9, 30 (ECGI Finance, Working Paper No. 422, 2014), available at <http://ssrn.com/abstract=2443792>.

27. Most scholars opposed defenses on the grounds that they thwarted takeovers, which were in their view beneficial in reducing agency costs between shareholders and directors. Some authors argued for a strict prohibition of any type of defenses to facilitate the proliferation of takeovers. This view is the so-called pure passivity

defenses and the pill was judicially challenged, Delaware courts ruled in favor of target companies, but they gave shareholders an out that may have initially appeared to balance the power in their favor.²⁸

Delaware judges allowed directors to adopt defensive measures so long as they can meet a two-prong test introduced in *Unocal Corp. v. Mesa Petroleum Co.* that requires that: (i) there are “reasonable grounds for believing that a danger or a threat to corporate policy exists” and (ii) “the response taken by the company . . . [is] reasonable in relation to the threat posed” (the latter is often referred to as the *Unocal* proportionality

standard. See, e.g., Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981) [hereinafter Easterbrook & Fischel, *Proper Role*]; Frank H. Easterbrook & Daniel R. Fischel, *Takeover Bids, Defensive Tactics, and Shareholders' Welfare*, 36 BUS. LAW. 1733 (1981) [hereinafter Easterbrook & Fischel, *Takeover Bids*]. Some other authors posit that while directors should be prohibited from obstructing takeovers through defenses, they should actively pursue alternative offers so that shareholders can benefit from higher takeover premiums. This view is the so-called modified passivity standard. See, e.g., Ronald J. Gilson, *Seeking Competitive Bids Versus Pure Passivity in Tender Offers Defense*, 35 STAN. L. REV. 51 (1982) [hereinafter Gilson, *Seeking Competitive Bids*]; Lucian A. Bebchuk, *The Case for Facilitating Competing Tender Offers*, 95 HARV. L. REV. 1028 (1982). Other authors critique auctions. See, e.g., Frank H. Easterbrook & Daniel R. Fischel, *Auctions and Sunk Costs in Tender Offers*, 35 STAN. L. REV. 1 (1982) [hereinafter Easterbrook & Fischel, *Auctions*] (explaining that auctions do not compensate a first bidder for its target search and therefore chill first bidders and acquisitions more generally); Alan Schwartz, *Search Theory and the Tender Offer Auction*, 2 J. L. ECON. ORG. 229 (1986) [hereinafter Schwartz, *Search Theory*] (explaining that auctions are detrimental as they turn the information a first bidder gathered about a target into a public good, thereby creating a disincentive to the search for targets and to acquisitions); see also Alan Schwartz, *Bebchuk on Minimum Offer Periods*, 2 J. L. ECON. ORG. 271 (1986) [hereinafter Schwartz, *Minimum Offer Periods*] (responding to Bebchuk's pro-auctions theories).

To be sure, several authors opposed the view that takeovers are beneficial and should not be discouraged. Martin Lipton, the inventor of the poison pill, has been historically one of the fiercest supporters of an approach that grants directors ample discretion to fight bids. See Martin Lipton, *Takeover Bids in the Target's Boardroom*, 35 BUS. LAW 101 (1979) [hereinafter Lipton, *Takeover Bids*]; Martin Lipton, *Corporate Governance in the Age of Finance Corporatism*, 136 U. PA. L. REV. 1 (1987) [hereinafter Lipton, *Corporate Governance*]; Lipton & Rowe, *supra* note 19. See also Kahan & Rock, *supra* note 25 (endorsing poison pills as a beneficial tool for shareholders because of greater premiums and a higher number of friendly deals); Jennifer Arlen, *Designing Mechanisms to Govern Takeover Defense: Private Contracting, Legal Intervention, and Unforeseen Contingencies*, 69 U. CHI. L. REV. 917 (2002); STEPHEN M. BAINBRIDGE, *MERGERS AND ACQUISITIONS* 352 (2003).

28. See *Unocal* at 493 A.2d at 959.

test).²⁹ The most important practical implication of the *Unocal* decision was on poison pills. In a subsequent case the Delaware Supreme Court used the *Unocal* test to validate the pill.³⁰ According to the Delaware judges, a pre-takeover defense like the pill raises fewer concerns than one adopted in the heat of an actual takeover battle because “pre-planning for the contingency of a hostile takeover might reduce the risk that, under the pressure of a takeover bid, management will fail to exercise reasonable judgment.”³¹ After all, the Delaware judges had explained in *Unocal* that the pill alone cannot determine the final outcome of the acquisition given that, “[i]f the stockholders are displeased with the action of their elected representatives, the powers of corporate democracy are at their disposal to turn the board out.”³² The

29. *Id.* at 955. With the crucial decision in *Unocal*, the Delaware Supreme Court established an intermediate standard of review between the entire fairness test (the rigorous standard for duty of loyalty cases) and the business judgment rule, which, according to Delaware judges, cannot apply in its pure form in takeover cases “[b]ecause of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders.” *Id.* at 954 (footnote omitted).

30. *See Moran*, 500 A.2d at 1346.

31. *Id.* at 1350.

32. *Unocal* at 493 A.2d at 959. This is not to say that this passage is the cornerstone of Delaware case law on defensive measures. After *Unocal* and *Moran*, several decisions over the last three decades have interpreted the *Unocal* proportionality standard with such deference to directors’ decisions that one might argue it has made the quoted *Unocal* passage less poignant than it was initially thought. *See Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48 (Del. Ch. 2011); *Third Point LLC v. Ruprecht*, 2014 Del. Ch. LEXIS 64 (Del. Ch. May 2, 2014). Note that this holds true even in the aftermath of the court’s decision in *Blasius Industries, Inc., v. Atlas Corp.*, 564 A.2d 651 (Del. Ch. 1988) and its progeny. Further, this requires a “compelling justification” for directors who seek to thwart the shareholder franchise. Unsurprisingly, attempts to thwart the franchise usually occur in connection with an M&A transaction requiring a shareholder vote. The primary basis for the *Blasius* decision was that the election of directors is “the ideological underpinning upon which the legitimacy of directorial power rests.” *Id.* at 659. Not only have Delaware Courts eroded the boundaries in which *Blasius*’ higher standard of compelling justification applies in favor of some other tests. *See Mercier v. Inter-Tel (Del.) Inc.*, 929 A.2d 786, 806-07 (Del. Ch. 2007) (formally applying the *Blasius* standard to a board decision not to delay a merger vote by twenty-five days when it became clear there were not enough votes in favor of the merger on the original meeting date, but holding that such standard must be consistent with the *Unocal* framework); *Keyser v. Curtis, C.A. No. 7109-VCN*, 2012 WL 311453, at *13 (Del. Ch. July 31, 2012) (applying an entire fairness test). Nevertheless, *Blasius* can do little when directors pre-plan thwarting the franchise well in advance of an M&A transaction.

court emphasized that even though the target directors won the specific battle, the takeover wars were far from over since shareholders retained, at least potentially, control on new battles to come. Delaware judges effectively moved the focus from tender offers to director elections.³³ When facing an unsolicited tender offer, directors can decide whether to preserve the company's independence and keep the poison pill in place, so long as a board can be ousted by a shareholder vote. In the language of Delaware courts today, that means so long as the target's response does not make "a bidder's ability to wage a successful proxy contest and gain control [of the board] . . . 'realistically unattainable.'"³⁴

Following *Moran*, pills became a fundamental component of U.S. corporate governance, and over the years targets have successfully resisted several attempts by shareholder plaintiffs to neutralize their reach.³⁵ As Professor Ronald Gilson put it, "the poison pill has become

33. Ronald J. Gilson, *Unocal Fifteen Years Later (And What We Can Do About It)*, 26 DEL. J. CORP. LAW 491, 500-01 (2001) (criticizing the choice by Delaware judges to prefer elections over market dynamics). See also Joseph A. Grundfest, *Just Vote No: A Minimalist Strategy for Dealing with Barbarians Inside the Gates*, 45 STAN. L. REV. 857 (1993).

34. This is the language the Delaware Supreme Court used in *Versata Enterprises v. Selectica, Inc.*, when it clarified how courts should interpret the *Unitrin* requirement by explaining that board responses must not be "preclusive." *Versata Enters., Inc. v. Selectica, Inc.*, 5 A.3d 586, 601 (Del. 2010) (citing *Carmody v. Toll Bros.*, 723 A.2d 1180, 1195 (Del. Ch. 1998)); see also *Airgas*, 16 A.3d at 113 (following the court's instructions when confronted with the *Unitrin* requirement).

35. Following *Unocal* and *Moran*, for a short period of time in the late 1980s the Chancery Court developed an interpretation of the *Unocal* test based on the allocation of powers between directors and shareholders in the decision on the outcome of a bid: absent a structurally coercive offer, that is, in the face of an all-cash, all-shares offer, where the only threat a board can claim is really price inadequacy and shareholder myopia (the latter, also known as "substantive coercion"), directors could not "just say no" and maintain the pill in place. Cf. *City Capital Assoc. v. Interco, Inc.*, 551 A.2d 787, 799-800 (Del. Ch. 1988) ("To acknowledge that directors may employ the recent innovation of 'poison pills' to deprive shareholders of the ability effectively to choose to accept a noncoercive offer, after the board has had a reasonable opportunity to explore or create alternatives or attempt to negotiate on the shareholders' behalf, would . . . be so inconsistent with widely shared notions of appropriate corporate governance as to threaten to diminish the legitimacy and authority of our corporate law."), *overruled by* *Paramount Commc'ns, Inc. v. Time, Inc.*, 571 A.2d 1140 (Del. 1990). However, this shareholder/bidder-friendly approach did not last long. In *Paramount Communications*, the Delaware Supreme Court overturned the *Interco* ruling when it made clear that a court cannot "substitut[e] its judgment as to what is a 'better' deal for that of a corporation's board of directors." *Paramount Commc'ns*, 571 A.2d at 1153. In

ubiquitous – every public company either has adopted a pill or can adopt one if a hostile offer is made.”³⁶ Indeed, one of the most important aspects of pills is that they can be adopted easily by the board: all companies have a poison pill plan “on-the-shelf” that can be approved quickly if and when circumstances so require.³⁷ The other very important characteristic of a poison pill, which I address further in Part III.B.2, is its “structural” nature:³⁸ the pill does not involve the taking of any action having financial or operational effect on the target—it solely acts as a deterrent on a bidder who will never decide to trigger it given its dilutive effects.³⁹ The absence of any financial or operational effects of such a defense allows stockholders to determine whether they want the tender offer to succeed without worrying about the long-term effects of the defense on the target stock.

the following decade, courts emboldened this pro-target reading of *Unocal*. In 1995, the Delaware Supreme Court decision widened the scope of board discretion in the face of an unsolicited bid. *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361 (Del. 1995). Under *Unitrin*, substantive coercion, which is the showing that shareholders could accept an inadequate offer because of “ignorance or mistaken belief[,]” was sufficient for directors to show the existence of a threat. *Id.* at 1385. In order to fail the second prong under *Unocal*, that is, the proportionality test, the board’s actions must be “draconian, by being either preclusive of coercive[,]” and, if the “response was not draconian, the Court must then determine whether it fell ‘within a range of reasonable responses to the threat’ posed.” *Id.* at 1367; *Airgas*, 16 A.3d at 92-93 (quoting *Unitrin*, 651 A.2d at 1367).

36. Gilson, *supra* note 33, at 501.

37. See John C. Coates IV, *Takeover Defenses in the Shadow of the Pill: A Critique of the Scientific Evidence*, 79 TEX. L. REV. 271, 289 (2000) [hereinafter Coates, *Takeover Defenses*]

[A]ll Delaware firms (except those few with other governance terms that would impede pill adoption) have had a shadow pill in place, witting or not. Takeovers of such firms have been restrained by a set of ‘shadow restrictions’—the expectation of a pill’s adoption and subsequent effects—on transfer of control to a hostile bidder. The adoption of an actual pill by any given firm only brings this shadow pill into the light, but does nothing to change the odds that the target will be acquired or not.

38. See *infra* Part III.B.2 and accompanying text for a definition of structural as opposed to transactional defenses.

39. See *id.* for a discussion of the “structural” nature of a poison pill.

B. ANTI-PILL SHAREHOLDER ACTIVISM IN THE EARLY 2000S

In the early 2000s, pills became unpopular among market participants. Most notably, pills lost their appeal to activist institutional investors⁴⁰ who began trying to bolster shareholders' control over corporate acquisitions by actually requiring that shareholders have a say not just at the proxy contest stage (the proxy contest in which they can replace the board with a new board that redeems the pill), but also at the stage of the pill adoption (or renewal).

Several non-binding stockholders' proposals on rights plans were put forward, typically requesting that a plan expire within a period of time (normally, no longer than one year) in the absence of stockholder ratification.⁴¹ The proxy firm Institutional Shareholder Services ("ISS") began issuing voting guidelines aimed at chilling the adoption or renewal of pills. In 2004, ISS recommended its clients, institutional shareholders of corporations, withhold their votes at the re-election of incumbent directors of a company if, following a company's previous annual meeting, a poison pill was approved or renewed by the company without shareholder approval.⁴² Starting with the 2010 proxy season, ISS recommended its clients vote against or withhold their votes for directors who voted (i) to adopt a pill with a term of more than twelve months, (ii) to renew a pill of any duration without shareholder

40. Compare MARIA CARMEN S. PINNELL, IRRC GOVERNANCE RESEARCH SERV., 2003 BACKGROUND REPORT E: POISON PILLS 1 (2003) (on file with author) (noting that starting in 2002 activists waged war against poison pills), and *Poison Pill Adoption on the Decline*, SHARKREPELLENT.NET (Oct. 3, 2003), https://www.sharkrepellent.net/request?an=dt.getPage&st=1&pg=/pub/rs_20031003.html&rnd=558416 (noting that "the increased efforts of shareholder activists along with an enhanced awareness of corporate governance issues resulted in 2003 setting a record for the number of shareholder proposals to redeem poison pills that have passed"), with John Laide, *Rethinking the Role of the Poison Pill?*, SHARKREPELLENT.NET (Sept. 17, 2008), https://www.sharkrepellent.net/pub/rs_20080916.html (noting how the trend against pills was actually experiencing a push-back in 2008 as companies felt more vulnerable given the depressed stock prices in the aftermath of the financial crisis).

41. There were seventy-eight non-binding proposals in 2003, forty-nine in 2004, and twenty-five by September 1, 2005. On each of those years the approval rate averaged around 60%. INSTITUTIONAL S'HOLDER SERVS., 2005 POSTSEASON REPORT: CORPORATE GOVERNANCE AT CROSSROADS 8 (2005) (on file with author).

42. INSTITUTIONAL S'HOLDER SERVS., US PROXY VOTING GUIDELINES SUMMARY app. D (ISS Proxy Voting Guidelines Summary) (2004) (on file with author).

approval, or (iii) to make a material adverse change to any existing pill without shareholder approval.⁴³

In parallel, activists sought to pass binding bylaw shareholder proposals on poison pills, whereby the bylaw would limit board powers with respect to poison pills and would not be subject to modification by the board without shareholder approval. A case in point was Professor Lucian Bebchuk's battle with CA, Inc. in 2006: the Harvard professor made a shareholder proposal for a bylaw to inhibit the board from adopting or maintaining a poison pill (other than by unanimous vote) and to limit the term of a board adopted plan to twelve months without shareholder approval.⁴⁴ After CA responded that the bylaw would not be valid under Delaware law, Bebchuk sued the company in Delaware for a ruling in favor of the bylaw. The Chancery Court ultimately dismissed the claim on procedural grounds as unripe for consideration, since the proposed bylaw had not yet been adopted.⁴⁵

In part because of pressure from shareholder activists, but also because – as John Coates demonstrated⁴⁶ – having or not having a pill in place during “peaceful times” is irrelevant since a company can always adopt one quickly after it becomes subject to an unsolicited acquisition attempt,⁴⁷ the overall number of companies with a traditional flip-in plan⁴⁸ in place significantly declined by the beginning of the 2010s. In

43. Matteo Tonello, *Poison Pills in 2011*, HARV. L. SCH. F. ON GOVERNANCE & FIN. REG. (Apr. 3, 2011, 9:49 AM), <http://blogs.law.harvard.edu/corpgov/2011/04/03/poison-pills-in-2011> (noting that, “[u]nder the revised guidelines, a director’s voting record on the company’s poison pill may factor into ISS’s recommendation concerning that director every time he or she is up for election[.]” whereas prior to those guidelines, “ISS would have made a voting recommendation only in the year that the pill was implemented or renewed.”). For a description of how effective ISS’s recommendations have been with respect to the way companies go about decisions on takeover defenses, see Coffee & Palia, *supra* note 22, at 17 (noting that “[o]ne measure of ISS’s influence is that most public companies in order to comply with ISS’s guidelines have either redeemed their poison pill or adopted a poison pill that is consistent with ISS’s guidelines (and thus has a duration of one year or less)”).

44. See Gordon Smith, *Bebchuk v. CA, Inc.*, CONGLOMERATE.ORG (June 16, 2006), http://www.theconglomerate.org/2006/06/bebchuk_v_ca_in.html (analyzing the *Bebchuk* ruling).

45. *Bebchuk v. CA, Inc.*, 902 A. 2d 737, 738 (Del. Ch. 2006).

46. See Coates, *Takeover Defenses*, *supra* note 37, at 287-88.

47. Cf. Coffee & Palia, *supra* note 22, at 79 (noting that companies might generally prefer to lay low rather than confronting a proxy advisor).

48. This Article primarily focuses on pills engineered to deter, obstruct, and restrict unsolicited takeovers. In corporate practice those are the flip-in plans. However, in the second half of the 2000s, companies started to adopt new types or variations of pills to

early 2011, less than 900 companies had a pill in effect (there were 2200 a decade earlier).⁴⁹

Thus, despite resistance from shareholder activists, management retains the ability to adopt poison pills quickly, even if the use of long-term pills has declined. At least in theory, shareholders do retain the ability to oust boards and their accompanying pills, a power that Delaware judges at least purportedly find meaningful; however, although Delaware judges expressed faith in shareholders' ability to exercise control in takeovers via director elections, directors made use of new devices external to the takeover regime. The most potent and most heavily debated of these new devices has been the use of staggered boards, to which I turn in Section I.C.

pursue goals other than fending-off hostile bids, such as: preserving a company's tax assets in the form of net operating losses. The so-called NOL pill, which was validated in *Versata*, aims to avoid an occurrence that would impair the tax asset, such as an "ownership change" for purposes of Section 382 of the Internal Revenue Code of 1986, as amended, by lowering the trigger of the pill to thresholds as low as 4.99% (as only shareholders beneficially owning at least 5% are generally considered for the ownership change analysis). *Versata Enters., Inc. v. Selectica, Inc.*, 5 A3d 586 (Del. 2010). Compare *id.*, with *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 8 (Del. Ch. 2010), in which two of the founders of Craigslist, Inc., for the express purpose of protecting the company's corporate culture, sought to implement a poison pill triggered, among other things, by an increase of ownership by a mere 0.01%. The court found that the preservation of corporate culture is not a valid threat under *Unocal*, and therefore such a poison pill is not valid. See generally Joseph M. Grieco, *The Ever-Evolving Poison Pill: The Pill in Asset Protection and Closely-Held Corporation Cases*, 36 DEL. J. CORP. L. 625, 637-44 (2011); Tonello, *supra* note 43, at 10-11 nn.14-25 and accompanying text; Bebchuk & Jackson, *supra* note 23, at 56.

49. See Tonello, *supra* note 43, at 10 nn.6-7 and accompanying text. Following Coates' suggestion, one should take this data with a grain of salt, especially if we consider that, only a few years ago, in the aftermath of the financial crisis, commentators and practitioners noticed a steep increase in the use of the pill for defensive purposes. Coates, *Takeover Defenses*, *supra* note 39. Indeed, with the collapse of financial markets around 2008 and 2009, companies believed their stock had become systematically undervalued and felt more vulnerable, considering how much cheaper it had become for an unsolicited bidder to grab a controlling block. See Laide, *supra* note 40; Jane K. Storer, *Poison Pills on the Rise . . . A Reaction to Shareholder Activism or a Signal of the Turbulent Financial Times?*, 12 NO. 2 M & A LAW. 17, 17 (2009).

C. TAKEOVER LEGAL BATTLES IN THE 2000S: BINDING BYLAW
SHAREHOLDER PROPOSALS ON POISON PILLS AND STAGGERED BOARDS

Over the last few years, the ever-animated legal and policy debate on takeover defenses and their long-standing effects on U.S. corporate governance – one of the most vehemently argued topics since the 1980s – has been, once again, at the forefront of corporate lawyers’ attention.

In the last decade, shareholder activists, mainly hedge funds and other institutional investors, sought to shake up Delaware rules on takeover defenses and, more generally, the allocation of powers between shareholders and directors. While ISS voting policies to dissuade directors from adopting pills were a response by market participants to pill boardroom practices,⁵⁰ other strategies raised new legal questions.

On one hand, the launch of binding bylaw shareholder proposals on poison pills triggered a debate on whether such devices are valid under Delaware law and whether embracing them would constitute sound corporate policy.⁵¹

On the other hand, the rise of a defensive tactic consisting of the combined use of poison pills and staggered boards caught the attention of leading scholars, who described it as a “powerful antitakeover force,”⁵² because it renders the winning of a proxy fight by a bidder – and therefore shareholder choice – insufficient to replace the majority of the board and redeem the pill. In a typical staggered board under Delaware law, with one-third of the directors coming up for reelection each year, in order to gain control of the board an insurgent would need to win two elections and as a result have to wait at least one year. This

50. The ultimate effectiveness of which is arguable, since directors have the ability to adopt pills subsequently on an as-needed basis.

51. See *infra* Part II.B on the allocation of decision-making powers between directors and shareholders; see generally Stephen M. Bainbridge, Director Primacy 7 (UCLA Sch. of Law, Law & Econ. Research Paper, No. 10-06, 2010), available at <http://ssrn.com/abstract=1615838> [hereinafter Bainbridge, Director Primacy]. (“[A] publicly held corporation’s decision-making structure is principally an authority-based one. ...[T]he statutory separation of ownership and control means that shareholders have essentially no power to initiate corporate action and, moreover, are entitled to approve or disapprove only a very few board actions. The statutory decision-making model thus is one in which the board acts and shareholders, at most, react.”).

52. This expression was coined by Lucian A. Bebchuk, John C. Coates IV and Guhan Subramanian in *The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence & Policy*, 54 STAN. L. REV. 887, 944 (2002) (proposing that “[c]ourts should not allow managers to continue blocking a takeover bid after they lose one election conducted over an acquisition offer”).

would “impose[] an additional and substantial cost that makes the ballot box route extremely difficult.”⁵³ Such devices kept academics and corporate practitioners busy until, in early 2011, the Delaware Chancery Court ruled in favor of the target directors in *Airgas*.⁵⁴

53. *Id.* at 923.

54. *Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48 (Del. Ch. 2011). In *Airgas*, the Delaware Chancery Court refused to compel the board of the target to redeem the pill following the bidder’s successful attempt to replace a slate of directors after a proxy fight. *Airgas* was widely publicized, in part, because Delaware courts decided not to invalidate takeover defenses that combine staggered boards and poison pills.

The extensive analysis by then-Chancellor William Chandler of how to apply the doctrines established by the Supreme Court of Delaware in *Unitrin*, and how to differentiate *Unitrin* from *Interco* built upon former Chancellor William Allen’s iconic statement in *TW Services, Inc. v. SWT Acquisition Corp.* that, “A corporation is not a New England town meeting; directors, not shareholders have responsibilities to manage the business and affairs of the corporation, subject however to a fiduciary obligation.” CIV. A. Nos. 10427, 10298, 1989 WL 20290, at *8 n.14 (Del. Ch. Mar. 2, 1989) (emphasis in *Airgas*, 16 A.3d at 102). See also *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361 (Del. 1995); *City Capital Assocs. v. Interco, Inc.*, 551 A.2d 787 (Del. Ch. 1988), *overruled by* *Paramount Commc’ns, Inc. v. Time, Inc.*, 571 A.2d 140 (Del. 1990). Following an analysis of the threat of inadequate price (the first prong under *Unocal*), the perils of an ownership structure that mutates following the announcement of a bid with the rise of arbitrageurs, based on prior opinions by the Supreme Court of Delaware (on which Chandler expressed some personal skepticism, yet acknowledged the nature of controlling precedents of such opinions), the Chancery Court ruled that the pill may be used with other defensive tactics and still be a reasonable response to a perceived threat—the pill may be “preclusive for now,” but not “preclusive forever.” *Airgas*, 16 A.3d at 104, 108, 113. Chancellor Chandler concluded that “[i]n order to have any effectiveness, pills do not—and can not—have a set expiration date. . . . This case . . . endorse[s] . . . Delaware’s long-understood respect for reasonably exercised managerial discretion, so long as boards are found to be acting in good faith and in accordance with their fiduciary duties” *Id.* at 129. The fact that the board was comprised of a majority of independent directors (including three directors nominated by the bidder, who ultimately voted in alignment with the fellow board members *not* to redeem the pill), played a crucial role in the determination that the response was not preclusive, given that, per *Unitrin*, it fell within a range of reasonableness.

Airgas was yet another victory for pro-management supporters who cite short-termism as a central concern of corporate law and call for further insulation of boards of directors from shareholder decision-making via corporate collateral factors such as staggered boards. See Lucian A. Bebchuk, *The Myth That Insulating Boards Serves Long-Term Value*, 113 COLUM. L. REV. 1637, 1653 (2013); see also Mark J. Roe, *Corporate Short-Termism — In the Boardroom and in the Courtroom*, 68 BUS. LAW. 977 (2013) for a critique of the call to diminish shareholders’ role in decision-making.

Rather than following the policy proposal that a staggered board should be compelled to redeem a pill if a bidder wins the first election and appoints one-third of the board,⁵⁵ *Airgas* has in fact confirmed the validity (at least for fact-patterns in which the newly-appointed directors vote in the same direction as the other incumbent directors)⁵⁶ of the “powerful antitakeover force” consisting of the combination of a staggered board with a poison pill. Delaware courts do not believe that such a combined device would make a proxy fight “realistically unattainable[,]” and, therefore, the defense cannot be considered “preclusive” to the launch of a proxy fight. Consequently, staggered boards and pills pass the validity test under *Unocal* and its progeny.⁵⁷

Nonetheless, the practical implications of such a decision are effectively limited to companies that already have a staggered board in place.⁵⁸

II. THE TAKEOVER PENDULUM IN DELAWARE: WOULD THERE EVER BE A “PRO-SHAREHOLDER DELAWARE”?

A. WHO TO DECIDE, DIRECTORS OR SHAREHOLDERS?

Thus far, the analysis shows how Delaware takeover law is still a hotly contested issue more than thirty years after the first wave of hostile bids in the 1980s. Despite the extensive debate, Delaware remains a

The role played by short-term oriented, deal-driven arbitrageurs in an attempted hostile acquisition such as *Airgas* is precisely the type of action pro-management advocates use as justification to support the use of corporate law collateral factors that alter the reversibility of a default regime. See *infra* note 66 and accompanying text.

55. Bebchuk, Coates & Subramanian, *supra* note 52.

56. It will be interesting to see if in the future a polarized staggered board will drive to a different outcome. In fact, one can wonder whether the *Airgas* judge would have reached the same conclusion if the directors elected by the bidder, instead of siding with the majority of the board in rejecting the offer, voted in favor of the bid and against maintaining the poison pill. To some extent, one can see that it was less problematic for the judge to rely on the business judgment of a board in which even the Air Products-elected directors did not believe the offer price was fair, than to overturn the board’s decision and compel redemption of the pill when no director thought it was in the best interest of the company and its shareholders.

57. In other words, Delaware courts validated structures that virtually insulate boards and make highly unlikely the chance that a bidder can singlehandedly remove the directors and redeem the pill, which *Unocal* initially left open as a viable hostile strategy for a bidder. See *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 959 (Del. 1985).

58. See *infra* Part III.B.1.e and III.C.

largely pro-target environment, and has not strayed from that path over the last three decades. This is not surprising when considered from a basic public choice perspective. Takeover law in Delaware is mainly made by judges who are well-aware of the potentially negative consequences for Delaware corporate law primacy of case law that sides with shareholders and bidders.⁵⁹ Indeed, the pill remains a cornerstone of American capitalism, and Delaware law remains highly deferential to boards. Even where its sole reason to oppose – in the *Unocal* taxonomy, the threat – is price inadequacy, whether real or alleged (i.e., shareholders' ignorance and mistaken belief regarding the stock's long-term value),⁶⁰ “a board that in good faith believes that a hostile offer is inadequate may ‘properly employ[] a poison pill as a proportionate defensive response to protect its stockholders from a ‘low ball’ bid’.”⁶¹

Takeover analysis is not limited to interpretation. In fact, it extends to the underlying merits and consequences of adopting one approach

59. Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588, 625-26 (2003) (mentioning the November 1988 Wachtell Lipton client alert memo, which was sent in the wake of the pro-bidder decision in *Interco* and advised its clients to consider reincorporating outside of Delaware should Delaware continue to rule against targets, which in fact did not happen); Roe, *Takeover Politics*, *supra* note 2, at 340-41, 353 (worried about the potential loss of primacy in the market for corporate charters, 1980s Delaware policymakers ruled for targets); Roberta Romano, *The Political Economy of Takeovers Statutes*, 73 VA. L. REV. 111, 120-22 (1987); Romano, *supra* note 21, at 467.

60. This often translates into “substantive coercion,” an expression introduced by Professors Ronald Gilson and Reiner Kraakman to describe a situation where (i) management actually believes the offer price is inadequate, and (ii) shareholders do not trust management's ability either to assess the circumstances objectively or to deliver on the expected long-term value. See Ronald J. Gilson & Reiner Kraakman, *Delaware's Intermediate Standard for Defensive Tactics: Is there Substance to Proportionality Review?*, 44 BUS. LAW. 247, 260 (1989). Substantive coercion was soon interpreted by the Delaware judiciary more loosely. See *Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48, 95-103 (Del. Ch. 2011); see also Guhan Subramanian, *Bargaining in the Shadow of Takeover Defenses*, 113 YALE L.J. 621, 633-35 (2003) for a critique of substantive coercion as a justification for director resistance to takeovers.

61. *Airgas*, 16 A.3d at 112-13. See *Paramount Commc'ns, Inc. v. Time, Inc.*, 571 A.2d 1140, 1150 n.12 (Del. 1990) (“The Supreme Court has unequivocally ‘endorse[d] the] conclusion that it is not a breach of faith for directors to determine that the present stock market price of shares is not representative of true value or that there may indeed be several market values for any corporation's stock.”); see also *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361, 1376 (Del. 1995) (“[T]he directors of a Delaware corporation have the prerogative to determine that the market undervalues its stock and to protect its stockholders from offers that do not reflect the long-term value of the corporation under its present management plan.”).

over the other. It includes consideration of (i) the pros and cons of binding pill shareholder bylaws; (ii) the pros and cons of combining pills and staggered boards; and ultimately, (iii) who should decide the fate of an unsolicited takeover attempt.

1. The Reasons for Letting Shareholders Decide

For many years now, a pro-shareholder approach, one in which directors must obtain shareholder approval to adopt or renew a pill (or any other defensive measure for that matter, which would in turn make the regime resemble those European jurisdictions that have adopted the board neutrality rule), has been advocated by scholars and shareholder activists and resisted by Delaware judges and most practitioners.⁶² Adherents to the pro-shareholder approach believe that letting shareholders determine the outcome of a contested acquisition is beneficial for several reasons, including that: (i) directors are conflicted and cannot express candid judgment as they face the risk of being replaced by the bidder;⁶³ (ii) the risk of director entrenchment is alleviated, which in the long run increases the likelihood of takeovers, which in turn curbs agency costs by forcing directors to maintain a high enough stock price to make an unsolicited acquisition less likely;⁶⁴ (iii) without board vetoes, and assuming mechanisms are in place to ensure undistorted choice by shareholders (i.e., a shareholder vote on the actual defense), the person who values the target the greatest is the most likely to seize corporate control, which is a desirable outcome from an

62. See *supra* note 27 and accompanying text.

63. This is the view reflected by those who endorse the so-called “pure passivity” approach (concluding that directors should stay passive and not erect any defenses in the face of a bid). See, e.g., Easterbrook & Fischel, *Takeover Bids*, *supra* note 27; Schwartz, *Search Theory*, *supra* note 27; Subramanian, *supra* note 60. This is also the view reflected by those endorsing the “modified passivity” approach (concluding that directors should erect no defenses other than seeking better offers and auctioning the company). See, e.g., Gilson, *Seeking Competitive Bids*, *supra* note 27; Bebchuk, *supra* note 27.

64. Henry Manne was the first prominent author who championed takeovers in the mid-1960s, precisely because of their disciplinary function. Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110 (1965). Fellow Chicagoans Judge Frank Easterbrook and Professor Daniel Fischel endorsed the disciplinary hypothesis years later. See Easterbrook & Fischel, *Takeover Bids*, *supra* note 27. Professor Subramanian takes a substantially similar approach. See also Subramanian, *supra* note 60.

efficiency standpoint;⁶⁵ and (iv) the absence of board vetoes increases M&A activity by forcing directors to consider acquisition proposals, which they would otherwise reject outright if they could veto the acquisition upfront. This increases the likelihood that deals will be ultimately negotiated and will promote better synergies and economies of scale and/or scope.⁶⁶

2. Do Directors Decide Better than Shareholders for Shareholders?

Conversely, those who support the current state-of-the-art in Delaware believe that any departure from the current rules would have a deep negative impact on corporate governance. Some supporters actually challenge the view that boosting takeover activity is beneficial.⁶⁷ Traditionally, opponents of shareholder-choice have argued that synergies and market-generated reactions against mismanagement only partially explain the takeover phenomenon. They maintain that acquisitions are inherently redistributive. As takeovers generate wealth, the wealth transfers to shareholders at the expense of creditors,⁶⁸

65. Lucian A. Bebchuk, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 HARV. L. REV. 1693, 1764-70 (1985) [hereinafter *Bebchuk, Toward Undistorted Choice*]; Lucian A. Bebchuk, *The Case Against Board Veto in Corporate Takeovers*, 69 U. CHI. L. REV. 973, 981-88, 991-94 (2002) [hereinafter *Bebchuk, Case Against Board Veto*].

66. See G. William Schwert, *Hostility in Takeovers: In the Eyes of the Beholder?*, 55 J. FIN. 2599, 2600 (2000) (noting that deals can change from hostile to friendly and vice versa); Subramanian, *supra* note 61, at 684, for a critique of the claim that friendly acquisitions in the United States are negotiated in the shadow of a hostile takeover bid; see also Edward B. Rock, *Adapting to the New Shareholder-Centric Reality*, 161 U. PA. L. REV. 1907, 1925 (2013) (noting that there were approximately three thousand friendly deals in the United States between 1996 and 2000, in comparison to only ninety-two hostile attempts in the same period: “[a]cademics’ stubborn focus on the ‘problem’ of managerial resistance to hostile takeovers is remarkable, considering the irrelevance of takeover defenses in a world in which managers are incentivized to think like shareholders.”). I believe that Rock’s remark is not conclusive, in that it is untestable: there is no way of knowing how many friendly deals would have occurred had Delaware (and other states) adopted a more shareholder friendly approach.

67. Lipton & Rowe, *supra* note 19, at 7 (“The opponents also observed that many hostile bids were opportunistic attempts to buy assets *on the cheap*, and that there was no empirical evidence that such takeovers were always (or ever) good for the economy.”) (emphasis in original).

68. See, e.g., Morrey W. McDaniel, *Bondholders and Corporate Governance*, 41 BUS. LAW. 413 (1986).

employees,⁶⁹ local communities,⁷⁰ target shareholders themselves,⁷¹ bidder's shareholders,⁷² and other stakeholders.⁷³ It is far from the purpose of this article to address whether any of these constituencies should – either under applicable law or from a policy perspective – be protected by directors. However, it is sufficient to say that under this line of reasoning, denying directors veto powers with respect to unsolicited takeovers would inundate companies and the market as a whole with acquisition activity, rendering them incapable of countering corporate raiders.

Over the years supporters of takeover defenses have gradually abandoned the position that directors should protect non-shareholder

69. See, e.g., Andrei Shleifer & Lawrence H. Summers, *Breach of Trust in Hostile Takeovers*, in CORPORATE TAKEOVERS: CAUSES AND CONSEQUENCES 33, 34-37, 41-42 (Alan J. Auerbach ed., 1988).

70. See, e.g., Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247 (1999).

71. Investor exploitation, by way of wealth transfers from target shareholders to the bidder, occurs as a result of several factors. One cause is the inherent pressure to tender that tender-offer mechanics structurally facilitate. See Lucian A. Bebchuk, *The Pressure to Tender: An Analysis and a Proposed Remedy*, 12 DEL. J. CORP. L. 911, 933 (1987) [hereinafter Bebchuk, *Pressure to Tender*] (noting that a shareholder vote, rather than defenses, should remedy such pressure). Another cause depends on the inability of the market to adequately price potential target corporations. This in turn can either depend on market myopia, noise, or inefficiencies, or it can occur because the potential target's stock price is systematically discounted compared to its fundamental value as a going concern. See, e.g., Robert J. Shiller, *Fashions, Fads, and Bubbles in Financial Markets*, in KNIGHTS, RAIDERS, AND TARGETS: THE IMPACT OF THE HOSTILE TAKEOVER 56 (John C. Coffee, Jr., et al. eds., 1988); Lipton, *Takeover Bids*, *supra* note 27; see also Reinier Kraakman, *Taking Discounts Seriously: The Implications of "Discounted" Share Prices as an Acquisition Motive*, 88 COLUM. L. REV. 891 (1988) for an example of the latter approach.

72. Bernard S. Black, *Bidder Overpayment in Takeovers*, 41 STAN. L. REV. 597 (1989) (explaining that managerial optimism, error, winner's curse, and agency costs often push a bidder to overpay at its stockholders' expense); James Fanto, *Braking the Merger Momentum: Reforming Corporate Law Governing Mega-Mergers*, 49 BUFF. L. REV. 249, 287 (2001) (explaining that peer pressure motivates CEOs to engage in acquisitions); Richard Roll, *The Hubris Hypothesis of Corporate Takeovers*, 59 J. BUS. 197 (1986) (discussing how decision-makers of the bidders tend to overestimate the value of targets at the expense of a bidder firm's shareholders).

73. But see Barry & Hatfield, *supra* note 26, at 659 (explaining that "[w]hile one might believe, a priori, that acquirers gain utility from takeovers at the expense of other parties—such as creditors, workers, customers (in the form of market power). . . , or the government (in the form of tax savings. . .)—empirical studies have generally found that these factors do not adequately explain takeover gains").

constituencies. They now primarily focus on shareholders' interests; namely long-term shareholder value.⁷⁴ In their view, without an adequate board response, targets would be subject to exploitation by bidders who would lure shareholders with premiums that do not fully represent the real value of the company, and could therefore acquire companies at lower prices.⁷⁵

In particular, as target's counsel argued in *Airgas*, a shareholder choice system would ultimately give arbitrageurs ("arbs") the final say on the fate of the company at the expense of long-term shareholders. Indeed, following the announcement of a bid, the ownership structure of a target typically changes. For example, in *Airgas*, instead of waiting for

74. See Lipton & Rowe, *supra* note 19, at 7; Dale A. Oesterle, *The Negotiation Model of Tender Offer Defenses and the Delaware Supreme Court*, 72 CORNELL L. REV. 117, 120-21 (1986); David D. Haddock et al., *Property Rights in Assets and Resistance to Tender Offers*, 73 VA. L. REV. 701, 705-06 (1987); see also Subramanian, *supra* note 60.

75. This is true even if the offer does not have any features of so-called structural coercion (e.g., a partial offer or a two-tier front-end loaded tender offer) that de facto disappeared from takeovers of U.S. companies in the aftermath of the takeover boom of the 1980s as a result of the invention of the pill, the case law validating defenses against structurally coercive offers, as well as, to a more limited extent, the federal intervention of the Williams Act and the SEC rules passed in the 1980s. See *supra* notes 18-22 and accompanying text. Consequently, the takeover market adopted typical coercive acquisition techniques, such as screening out partial bids. Subsequently, the takeover market permitted shareholders to tender their shares during the "second round of tendering" even after the bid period has closed. This technique suppresses any pressure on the shareholder to tender (with an option to tender the shares in the second round, a shareholder who opposes the bid can wait until the first round of offers closes and will decide to tender only if the offer ultimately succeeds; without an option to tender in the second round, that same opposing shareholder would have been pressured to tender by the risk that the offer succeeds and he or she gets stuck with minority shares). Second rounds are generally mandatory under U.K. regulation, unless an offer is unconditional as to acceptances from the outset. See PANEL ON TAKEOVERS AND MERGERS, THE CITY CODE ON TAKEOVERS AND MERGERS, Rule 31.4, at N1 (11d ed. 2013), available at <http://www.thetakeoverpanel.org.uk/wp-content/uploads/2008/11/code.pdf>. They have been imported as best practice in the U.S. pursuant to SEC Rule 14d-11 under the Williams Act. See generally Bebchuk, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, *supra* note 65, at 1797-98 (noting how second rounds involve free-rider problems, in that more than a stockholder who approves of the offer would rather wait and to see the results of the offer and only at that point would decide whether to tender: this is because of the transaction costs associated with tendering during the first round and not having the stock available in the interim period).

a potentially greater, yet undetermined, offer price, a substantial amount of shareholders chose to cash-in by selling to arbs at the post-announcement market price.⁷⁶ Shareholders receive smaller premiums

76. The arbs story played a significant role in *Airgas* where, following the announcement of the takeover by Air Products, arbs and other event-driven investors started to purchase significant stakes in the target stock that ultimately allowed them to own approximately 46% of the company. *Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48, 118 (Del. Ch. 2011). “Airgas’s board members testified that the concepts of coercion, threat, and the decision whether or not to redeem the pill were nonetheless ‘implicit’ in the board’s discussions due to their knowledge that a large percentage of Airgas’s stock is held by merger arbitrageurs who have short-term interests and would be willing to tender into an inadequate offer.” *Id.* at 105.

Short-term oriented investing as represented by event-driven, merger arbitrageurs is central to understanding pro-target advocates’ support for anti-takeover measures like poison pills, staggered boards, and delayed shareholder elections. Much of the debate in corporate law regarding board-insulation revolves around the problem of short-termism. Since the inception of the 1980s takeover boom, Martin Lipton, the most prominent voice in management advocacy, has been citing investors’ short-termism as a primary justification for empowering directors with veto power in the context of hostile acquisitions. *See, e.g.*, Lipton, *Takeover Bids*, *supra* note 27, at 104-05. Lipton argues that the policy debate regarding corporate governance should be framed as: “[w]hether the long-term interests of the nation’s corporate system and economy should be jeopardized . . . to benefit speculators” only interested in quick profits. *Id.* at 104 (emphasis omitted). Insulating boards of directors from shareholder pressure, and thus limiting shareholder voice, the argument goes, best serves the long-term interests of the corporation and its long-term shareholders. *See also* Stephen M. Bainbridge, *Director Primacy and Shareholder Disempowerment*, 119 HARV. L. REV. 1735, 1744-51 (2006). *But see* Bebchuk, *supra* note 55, at 1637 (using empirical evidence to argue against the conventional short-termist arguments supporting board insulation via poison pills and corporate law collateral factors).

In *Airgas*, short-termism concerns played an important role in the court’s ultimate decision to allow the board of directors to maintain the poison pill despite having lost the first election. *Airgas*, 26 A.3d at 108-12. Central to the court’s decision was testimony from experts on both sides of the legal battle that short-term arbs “would be happy to tender their shares at [the offer] price regardless of the potential long-term value of the company.” *Id.* at 111; Roe, *supra* note 54, at 990 (detailing then-Chancellor Chandler’s analysis regarding the role of short-termism and deal arbs in *Airgas*). Perhaps not surprisingly, other members of the Delaware judiciary have expressed concerns over investor short-termism in extrajudicial writings. Delaware judges (former and current) have stressed in scholarly articles the dangers of short-termism and the need to further insulate boards of directors for long-term benefits. *See* Jack Jacobs, “Patient Capital”: *Can Delaware Corporate Law Help Revive It?*, 68 WASH. & LEE L. REV. 1645, 1649-50 (2011) (expressing concern over short-term oriented investors and their effect on long-term value creation); William T. Allen, Jack B. Jacobs & Leo E. Strine, Jr., *The Great Takeover Debate: A Mediation on Bridging the Conceptual Divide*, 69 U. CHI. L. REV. 1067, 1096-100 (2002) (proposing triennial director

when they act prematurely, but early action effectively transfers the deal consummation risk to the arbs, who will not realize a benefit unless the deal closes. Pro-target advocates argue that fostering shareholder-choice in takeovers only protects the arbs, who care more about deal consummation than the long-term value reflected in the price ultimately paid by the bidder.

B. CAN SHAREHOLDERS DECIDE ANYTHING AT ALL?

An important aspect of Delaware's management-friendly, pro-target legal environment, particularly in light of the recent debate on shareholder pill bylaws, is that opponents of a shareholder-choice system would not allow a company to adopt restrictions on pills voluntarily without board confirmation, as shareholders alone cannot legislate to that effect in the bylaws.⁷⁷ While boards may adopt these

elections to mitigate short-termism issues and foster long-term value creation); Leo E. Strine, Jr., *One Fundamental Corporate Governance Question We Face: Can Corporations Be Managed for the Long Term Unless Their Powerful Electorates Also Act and Think Long Term?*, 66 BUS. LAW. 1, 1-3 (2010) (discussing the tension between short-term investment horizons and the long-term best interests of corporations); Leo E. Strine, Jr., *The Delaware Way: How We Do Corporate Law and Some of the New Challenges We (and Europe) Face*, 30 DEL. J. CORP. L. 673, 687-90 (2005) (discussing concerns over short-termism in relation to corporate takeover policy).

77. Delaware corporate law is generally comprised of enabling rules out of which private parties can contract; however, some authors suggest that Section 141(a) of the *Delaware General Corporation Law* ("DGCL") requires that a board decision on the bid (and on the defenses to fight it) be taken *at the actual time of the bid* and that any imposition by a shareholder bylaw to tie directors' hands for the future would run afoul of such rule, in that directors would not be in a position to discharge their duties freely at the time the corporation faced a hostile bid. DEL. CODE ANN. TIT. 8, § 141(a) (2014). See Stephen M. Bainbridge, *Director Primacy in Corporate Takeovers: Preliminary Reflections*, 55 STAN. L. REV. 791 (2002) [hereinafter Bainbridge, *Preliminary Reflections*]; see generally Bainbridge, *Director Primacy*, supra note 52, at 7 (noting that of the two extremes of the decision-making models, publicly held corporations principally tend to operate on an authority-based platform, leaving shareholders with little power); *CA, Inc. v. AFSCME Emps. Pension Plan*, 953 A.2d 227, 232-35 (Del. 2008) (noting that limits to directors' managerial powers under Section 141(a) of the DGCL need a "specific authorization in either the statute or the certificate of incorporation"). This is a peril that does not seem to bother shareholders' advocates who argue that if the bid were not high enough, shareholders would authorize the board to adopt the pill. Their critics' rebuttal is that typically, at the time the bid is presented, the shareholder base is largely comprised of arbs whose long positions were created in anticipation of an upcoming sale of shares regardless of the adequacy of the presented

restrictions on their own,⁷⁸ they have never done so, at least expressly in terms of binding and irrevocable commitments with respect to future pill adoption, maintenance, or renewal;⁷⁹ under pressure from institutional investors, the farthest they normally go is simply not renewing a pill or redeeming an existing one,⁸⁰ but they do not tie directors' hands indefinitely.

This debate largely misses a critical nuance: the anti-takeover regime itself plays a role that is not as important as scholars have portrayed it. Consider the following: *if* Delaware judges, contrary to the body of case law they built since the 1980s, allowed shareholders alone to take those steps, Delaware would resemble the European system under the European Takeover Directive.⁸¹ Should a pro-shareholder approach be endorsed, shareholders of Delaware companies would be able, if such bylaws were actually approved, to opt into a regime similar to the board neutrality rule, which imposes managerial passivity unless shareholders approve the defenses.⁸² In other words, the regime proposed by pro-shareholder advocates would make Delaware similar to

price. Those short-term investors are allegedly indifferent to the target's fundamental or long-term value because they only care about their ability to remove the board and tender their shares. *See, e.g., Airgas*, 16 A.3d at 108-10.

78. To be sure, to make it a credible commitment directors would also have to set up some mechanism to ensure the board could not subsequently reverse this newly-adopted system. For example, as soon as a bid is perceived as imminent—otherwise, the whole purpose of such commitment would be defeated. Such a mechanism could be achieved through hardwiring (e.g., by allowing its reversal only with shareholder consent) or through an outright prohibition to reverse it (possibly subject to a sunset after a certain number of years), as an indeterminate and non-reversible commitment might be considered in violation of the DGCL and the ensuing case law on pills based on Section 141(a). *See DEL. CODE ANN. TIT. 8, § 141(a); Quickturn Design Sys. v. Shapiro*, 721 A.2d 1281, 1293 (Del. 1998) (holding that a “Delayed Redemption Provision” in a so-called “dead-hand” pill is invalid because it “impermissibly circumscribes the board’s statutory power under Section 141(a) and the directors’ ability to fulfill their concomitant fiduciary duties”).

79. But they still can make hostile offers more or less probable through several other ways (e.g., by adopting a staggered board). *See, infra* Part III.B.1.a.

80. *See Tonello, supra* note 43.

81. *See supra* note 6.

82. More precisely, the Directive gave EU Member States the option to decide whether to impose the board neutrality rule as mandatory. If a Member State does not impose the board neutrality rule, companies can revert to the “default” regime and adopt the rule on a voluntary basis. *See supra* note 6 and accompanying text.

those European jurisdictions⁸³ that by default do not impose the board neutrality rule, but instead make it optional for shareholders to adopt it (the Directive requires Member States to leave the door open to such opt-in if they do not impose the board neutrality rule).⁸⁴ However, given the public choice-type dynamics behind Delaware rulemaking (especially after the *Airgas* decision, in which such dynamics are more than apparent),⁸⁵ one should not expect to see this happening anytime soon.

Still, with the caveats I describe shortly, from a takeover law perspective, the vast majority of Delaware companies facing unsolicited bids are ultimately in a situation that does not significantly differ from the regime their European peers are subject to with the board neutrality rule. The rest of this article explains why and how.

III. DO THE LAWS ON TAKEOVER DEFENSES MATTER?

Before taking on the main thesis of this article,⁸⁶ it is beneficial to consider its background. Mainstream literature (from both academic and

83. That is the regime of, among others, Germany, the Netherlands, Belgium, and Poland. See CTR. EUROPEAN POLICY STUDIES, THE TAKEOVER BIDS DIRECTIVE ASSESSMENT REPORT 190 (2012), available at http://ec.europa.eu/internal_market/company/docs/takeoverbids/study/study_en.pdf [hereinafter CEPS REPORT].

84. See Council Directive 2004/25, art. 12, 2004 O.J. (L 142) 21 (EC).

85. In *Airgas*, then-Chancellor Chandler did not refrain from criticizing Delaware's current pro-target jurisprudence. However, he recognized he had little room to maneuver for a ruling favorable to the bidder, as the Delaware Supreme Court would have likely overturned any departure from the state-of-the-art in Delaware. *Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48 (Del. Ch. 2011). Therefore, as Steven Davidoff characterized the decision, then-Chancellor Chandler decided "strategically" in favor of the target's board. Steven M. Davidoff, *Air Products v. Airgas and the Value of Strategic Judicial Decision-Making* 2012 COLUM. BUS. L. REV. 502, 505-07 (2012). This is very much in line with Professor Roe's analysis of Delaware politics: its judiciary is aware that any pro-bidder decision would put its primacy at risk. Roe, *supra* note 60, at 625-26. Furthermore, this is actually similar to what happened in the 1980s in the aftermath of two of the rare decisions in which judges ruled against directors. *City Capital Assocs. v. Interco, Inc.*, 551 A.2d 787 (Del. Ch. 1988); *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985), *overruled by Gantler v. Stephens*, 965 A.2d 695 (Del. 2009).

86. The basic idea I wish to further develop in this Article has been first introduced in an earlier work of mine. MATTEO GATTI, OPA E STRUTTURA DEL MERCATO DEL CONTROLLO SOCIETARIO [TENDER OFFERS AND THE STRUCTURE OF THE MARKET FOR CORPORATE CONTROL] 96-107 (2004) (drawing from intuitions present in Matteo Gatti,

practicing lawyers) has traditionally consisted of two types of discussion: (i) the positive law debate as to whether under applicable law shareholders (as opposed to directors) have power to decide on the outcome of the acquisition; and (ii) the policy debate as to whether shareholders (as opposed to directors) *should* have such power. In the rest of this article, I show that under both the current Delaware and United Kingdom regimes, shareholders do have such power, yet sometimes they are in no position to exercise it—and the reason for such inability to exercise such power is not embedded in the takeover regime, but rather in rules, principles and/or practices that are external to it – what I call corporate law collateral factors. My purpose is to show (i) who *actually* has power in a takeover situation; and (ii) what rules, principles and/or practices (external to the takeover regime) are at work to bestow such power. The policy implications are quite intuitive: commentators pushing for more shareholder power in the takeover context need not look at and change the takeover regime itself but rather

Limitations of Acquirers' Contractual Freedom in the Market for Corporate Control 45-50 (2002) (unpublished LL.M. Paper, Harvard Law School) (on file with author)); see Luca Enriques & Matteo Gatti, *EC Reforms of Corporate Governance and Capital Markets Law: Do They Tackle Insiders' Opportunism?*, 28 NW. J. INT'L L. & BUS 1, 29 n.144 (2007). The idea has since been developed by some European scholars. See also Carsten Gerner-Beuerle, David Kershaw & Matteo Solinas, *Is the Board Neutrality Rule Trivial? Amnesia about Corporate Law in European Takeover Regulation*, 22 EUR. BUS. L. REV. 559, 562 (2011). While Gerner-Beuerle, Kershaw, and Solinas' article is a step forward in the development of the idea and its contribution to the literature, the focus of that work is centered around Europe and the Member States' implementation of the Takeover Bids Directive in relation to the board neutrality rule: one of their main points is that, even absent a board neutrality rule, most European companies would not be truly free to implement defenses because of restrictions under national company laws, and in such circumstances the takeover regime itself is inconsequential. Aside from focusing more on takeovers on this side of the Atlantic, in this Article I develop the idea from a different perspective: my starting point is that Delaware and the United Kingdom are really not that different, but for the aforementioned corporate law collateral factors, and each regime becomes *actually relevant*—as opposed to trivial—precisely because those factors are at work. In other words, the very presence of corporate law collateral factors indicates that the takeover regime does matter, and that picking one regime over the other can lead to certain consequences from a policy standpoint. Essentially, the attainment of whatever policy goals a legislature intends to pursue should be netted out of any unintended effects such corporate law collateral factors might contribute or, if the legislature is ultimately comfortable with such factors playing a role, that decision should expressly be made when the takeover rules are set (or interpreted).

such external rules, principles and/or practices (and their combination with such regime).

A. JUST A DIFFERENT “DEFAULT” REGIME?

If Delaware decided to change the allocation of power between directors and shareholders in the context of hostile acquisitions, its takeover laws would be similar to those of certain European jurisdictions. That would be a catastrophic departure from a well-established body of law according to some,⁸⁷ while others would welcome it as a major improvement.⁸⁸ I question whether, even without such a change, the status quo in Delaware is so drastically different from the pro-shareholder regime in the United Kingdom.

In fact, as some authors have conceded, the Delaware system and a regime of board neutrality are similar: under both, shareholders have the ability to determine the outcome of an acquisition.⁸⁹

In Delaware, a bidder can mount a proxy fight to oust the incumbent directors, replace them with new ones who will redeem the poison pill and allow the acquisition to go through: if enough shareholders are convinced the price the bidder is offering adequately values their shares, they will vote in favor of the bidder's candidates and reverse the pro-target Delaware regime.⁹⁰

Conversely, in the United Kingdom as well as in several other European Union (“EU”) jurisdictions there is a specular, but arguably still similar, situation: directors need to get shareholder approval to fend off a bid.⁹¹ They need to convince shareholders that the offer on the

87. See, e.g., Lipton & Rowe, *supra* note 19, at 3 (noting that adopting this method would be a huge departure from precedent); Bainbridge, *Preliminary Reflections*, *supra* note 77, at 794; Bainbridge, *Director Primacy*, *supra* note 51, at 3, 13-14.

88. See generally Lucian A. Bebchuk, *Letting Shareholders Set the Rules*, 119 HARV. L. REV. 1784 (2006) (positing that granting shareholders greater power would be favorable); Bebchuk, *supra* note 66.

89. Bebchuk & Hart, *supra* note 8, at 4.

90. *Id.*

91. See PANEL ON TAKEOVERS AND MERGERS, THE CITY CODE ON TAKEOVERS AND MERGERS, Rule 21, at 114 (11d ed. 2013), available at <http://www.thetakeoverpanel.org.uk/wp-content/uploads/2008/11/code.pdf> (United Kingdom); Article 104, of the so-called Consolidated Financial Act (Legislative Decree no. 58 of February 24, 1998, Supp. Ord. no. 52/L to Gazz. Uff. no. 71 of March 26, 1998, as last amended by Legislative Decree no. 104 of July 2, 2010, Supp. Ord. no. 148/L to Gazz. Uff. No. 156 of July 7, 2010) (It.) (the provision allows opt-out). Note that until 2014, France was

table is not in their best interests; if enough shareholders do not like the bid, the board will be granted authority to adopt defenses to reject the low-ball bid.

Under both regimes, with a vote in one direction or the other, shareholders can have a critical, often times determinant, say on whether the tender offer should succeed or not. The real difference between the two seemingly opposite regimes rests upon the beneficiary of shareholders' inertia, that is, whom the regime favors if no shareholder vote occurs.

In the Delaware system, the regime is advantageous to target directors: in the absence of a proxy fight, the board may maintain the pill in place (or adopt it if it does not have one already), thus deterring a bidder from an unsolicited acquisition attempt. Instead, the U.K. system favors bidders: absent a shareholder vote, a target cannot erect defenses and obstruct a bid.

But even if these two regimes initially favor different sides of the takeover battle, the fact that shareholders can vote to reverse the applicable regime may ultimately make the debate on how to allocate corporate power moot. After all, if the real difference between the two systems is who the default rule initially favors, because under both regimes shareholders are in the position to decide on the outcome of the bid, the overall issue ceases to seem that relevant and one may question whether adopting one or the other has any impact.⁹²

one of the jurisdictions that had adopted the board neutrality rule. *See* Loi 2006-387 du 31 mars 2006 relative aux offres publiques d'acquisition [Law 2006-387 of March 31, 2006 on Public Offers], JOURNAL OFFICIEL DE LA REPUBLIQUE FRANCAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], Apr. 1, 2006, art. 12. Article 10(V) of Loi 2014-384 of March 29, 2014 converted the board neutrality rule into an opt-in provision.

92. The typical default rules in corporate codes are generally considered somewhat sticky. *See* Luca Enriques, Ronald J. Gilson & Alessio M. Paces, *The Case for an Unbiased Takeover Law (with an Application to the European Union)* 5 (Stanford Law Sch., John M. Olin Program in Law & Econ. Working Paper Series, Paper No. 444, 2013), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2258926. Nevertheless, I am not convinced that in a system of shareholder approval in the face a takeover, the stickiness of what I call default is actually relevant *in the absence of other factors outside of the takeover regime*. *See supra* note 10 for a description of my use of the term default. *See infra* Part III.B for a discussion of what really matters in the absence of such other factors. In Delaware, once a bidder decides to pursue a target, it will consider all its options to get through the finish line, including, if it has to, going hostile, replacing the board and redeeming the pill. After all, the situation is not that different to when an acquirer has to take some extra steps in the structuring of a transaction in order to win a target. Consider an acquisition, whether hostile or friendly

B. HOW REVERSIBLE ARE THE DELAWARE AND THE U.K. REGIMES? JUST
ASK CORPORATE LAW

Two apparently different regimes on takeover defenses, the *Unocal* doctrine and its progeny in Delaware and the board neutrality rule in the United Kingdom, have a common feature, which is shareholders' ability to have a critical (if not determinant) say on an unsolicited acquisition attempt. Despite this similarity, the two regimes differ in the beneficiary of the default they set forth (targets in Delaware and bidders in the United Kingdom). In Section A, I suggested that one could legitimately doubt whether the two regimes are any different, since takeover actors can expect shareholders' preferences to drive the final outcome of the acquisition regardless of where the default regime is initially set. One could even consider the choice of default regime as not significant.

The conclusion that the two systems are ultimately similar and not significant rests on the basic assumption that each regime is reversible without much difficulty or expense. Therefore, for the two default regimes to matter in the outcome of an acquisition contest, their *degree of reversibility* is crucial: if the parties interested in reversing the status quo find undue burdens and do not have a fair chance to prevail, setting the default one way or the other will have a significant impact on the final outcome, since the default rule will less likely be reversed.⁹³

Sometimes, such an assumption cannot be met; that is not a result of the takeover regime itself, but rather derives from certain corporate law rules, principles and/or practices applicable in the particular jurisdiction. In other words, without such rules, principles and/or practices, which are external to the takeover regime and labeled here as "corporate law collateral factors," the two regimes could, from an

is irrelevant, of companies whose financing contracts contain change-in-control provisions: it is customary that, in parallel to the acquisition piece of the transaction, the acquirer would make an exit consent-type tender offer on the corporate debt as well. In other words, in the M&A world acquirers have to go to extra lengths quite often, so the fact that a proxy contest might be necessary should not really alter the final outcome if the proxy rules and other factors do not make it overly difficult for the acquirer to win control of the board. Similar considerations apply to the opposite regime of board passivity, where the board can actually play a crucial role, given the control of the proxy machinery, to convince shareholders to approve defenses when a low-ball offer is on the table.

93. Cf. Bebchuk & Hart, *supra* note 8, at 4 (noting that "[p]oison pills can become problematic . . . when combined with arrangements that make it difficult or even impossible for a rival to get an effective shareholder vote on its acquisition offer").

aseptic legal perspective, be reversed with very similar odds.⁹⁴ Whenever reversibility of the takeover regime is guaranteed, this Article argues that the legal regime would determine the outcome of a bid much less than other real-world considerations, such as the actual ownership structure of the target, the premium offered by the bidder, the intensity of the efforts by target and bidder to prevail in the takeover, as well as their ability to shape the best takeover strategies from legal, business, financial, and public relations perspectives.

This Section analyzes the reversibility of a default regime from the perspective of regimes, like those in Delaware and the United Kingdom, on two distinct conceptual levels, by looking at (i) the rules, principles, and practices governing shareholder voting, director elections, and board composition,⁹⁵ and (ii) the type of defenses that can ultimately be chosen by a target's board to fend off a tender offer under each regime (IV.B.2).⁹⁶ Sub-section one addresses technical aspects of shareholder voting and elections, while sub-section two relates to the spectrum of choices for shareholders (and how those choices appeal to them). Each is a corporate law collateral factor of a very different nature.⁹⁷

1. Board Composition, Directors' Elections, and Shareholder Voting

Rules governing board composition, director elections, and shareholder voting generally are the most relevant factors affecting the reversibility of a takeover regime giving shareholders a say in the outcome of an acquisition. I separately analyze staggered boards, director removability, shareholders' ability to call special meetings or act by written consent, supermajority provisions, proxy rules in general,

94. Such rules, principles, and/or practices happen to produce collateral effects on the takeover regime and the potential outcome of an acquisition, even if the primary rationale for such a rule, principle, or practice is not to influence the outcome of an acquisition.

95. See *infra* Part III.B.1.

96. See *infra* Part III.B.2.

97. This Article does not address corporate law factors that do not affect the reversibility of the anti-takeover regime; it only addresses those that affect the general contestability of control of a given target. The two issues are rather different, and the former does not matter for current purposes. This Article deals with corporations that are (or can become) subject to a hostile takeover, that is, corporations whose control is contestable in the market. Corporations whose control is not contestable in the market for whatever reasons, including ownership structure and/or pre-bid defenses, are not the focus here. Therefore, the Article does not analyze, among other things, dual-class share structures, pyramidal groups, and cross-shareholding.

and rules policing shareholders' conflicts of interest. Preliminarily though, some context on the role played by shareholder voting in the acquisitions context will set the stage for the analysis.

Shareholder voting is considered by some scholars an effective way to solve the pressure-to-tender problem affecting tender offers: in short, the concern that shareholders might decide whether to tender their shares not on the basis of the merits of the offer, but rather because they want to avoid failing to tender to an offer that is ultimately successful, in which case they would get stuck with minority shares that would trade at a much lower price.⁹⁸ By way of voting, shareholders are able to decide cohesively, as if they were a "sole owner" who can evaluate all the pros and cons of a given proposal.⁹⁹ The decision reached by shareholders is considered the best tool a legal system can provide to obtain a statistical approximation of what a sole owner would have done in a two-person, buyer and seller negotiation.¹⁰⁰ In the absence of a vote, shareholders would fail to coordinate and might likely decide to tender because of pressure to do so. Since shareholders are able to tender their shares even if they voted against the bid, when they vote they can express their genuine opinion of the bid based on how they view the offer price versus the expected value of the target should it stay independent. To put all this in the context of the two systems: in Delaware, shareholders who do not want the bid to succeed will vote for the incumbent directors who will maintain the pill in place; in the United Kingdom, those same shareholders would cast their votes to authorize directors to adopt defenses.

98. Professor Bebchuk is the most prominent advocate of shareholder voting in acquisitions. See Bebchuk, *supra* note 65; Bebchuk, *Pressure to Tender*, *supra* note 71; Lucian A. Bebchuk, *The Sole Owner Standard for Takeover Policy*, 17 J. LEG. ST. 197 (1988).

99. Lucian A. Bebchuk, *A Model of the Outcome of Takeover Bids* 16, 22 (Harvard Law Sch., John M. Olin Ctr. Law, Econ. & Bus., Discussion Paper No. 11, 1985) (on file with author). See also Zohar Goshen, *Voting (Insincerely) in Corporate Law*, 2 THEORETICAL INQUIRIES L. 815, 835 (2001) ("These restrictions [including shareholder voting] allow security holders to arrive at the group preference by forcing people who wish to transact with the group to acquire its consent. . . . [T]ransactions are invalid *ex ante* if the rights of the security holders are not protected up front.").

100. See Zohar Goshen, *The Efficiency of Controlling Corporate Self-Dealing: Theory Meets Reality*, 91 CAL. L. REV. 393, 399-400 (2003); see also Bebchuk, *Pressure to Tender*, *supra* note 72, at 915-17 (discussing the actions of a sole owner in the sale of his or her assets and why the shareholder vote is the best mechanism to ensure undistorted choice and efficient allocation of assets in a tender offer).

The following subsections *a.* through *f.* will analyze instances in which shareholder choice cannot genuinely show the group preference on a tender offer, namely, when a staggered board is in place, when there are obstacles to director removability, when shareholders cannot call special meetings or act by written consent, when a supermajority is required to pass the relevant resolution, unbalanced proxy rules and ineffective policing of shareholders' conflict of interest.

While, admittedly, legal commentators have given broad attention to staggered boards over the last ten to fifteen years, many other significant corporate law collateral factors have largely been overlooked.

a. Staggered Boards

When combined with a staggered board, a pro-target regime is very likely to favor the target company. In Delaware, staggered boards alter the outcome of proxy fights contests aimed at ousting the board and removing anti-takeover devices, such as the poison pill.¹⁰¹ In order to replace the majority of the board and redeem a pill, a bidder would need to win two elections within a one-year interval.¹⁰² As leading scholars have demonstrated, this is quite problematic, as at the first election bidders will effectively give target shareholders a put option exercisable one year later: if between the two elections the stock has gone down, the bidder will have to close an acquisition where it is likely overpaying (the stock has gone down at a time when the bidder had only one-third of the board and could not run the company); if, however, the target stock has gone up, shareholders (meaning, M&A arbitrageurs) would likely not vote for the bidder nominees unless the bidder increases the initial offer

101. Bebchuk, Coates & Subramanian, *supra* note 52, at 890. Significantly, commentators have proposed reforms to further insulate boards within the pro-target default regime by requiring intervals between director elections of greater than one year. These proposals are primarily driven by short-termism concerns. See Martin Lipton & Steven A. Rosenblum, *A New System of Corporate Governance: The Quinquennial Election of Directors*, 58 U. CHI. L. REV. 187, 224-31 (1991) (proposing intervals of five-years); Jacobs, *supra* note 77, at 1658 (proposing intervals of five-years); Allen, Jacobs & Strine, *supra* note 77, at 1072 (proposing intervals of three-years); see also Guhan Subramanian, *Delaware's Choice*, 39 DEL. J. CORP. L. 1, 9-12 (2014) (proposing as an alternative to the current trend of declassifying staggered boards, three-year terms for boards of directors of ineffective staggered boards, for example a "bylaws-based" staggered board, with the ability for shareholders to "recall" the directors if a hostile takeover bid is presented).

102. Bebchuk, Coates & Subramanian, *supra* note 52, at 890.

(why change course if the market likes the current board?).¹⁰³ All in all, staggered boards make unsolicited deals less likely. Not surprisingly, one empirical study has shown that the stock market responds positively to the potential destaggering of the board and negatively when the staggered board is maintained.¹⁰⁴

In sum, the proposition that the takeover regime does not matter does not hold for Delaware companies that have an effective staggered board.¹⁰⁵ It is no wonder that the staggered board has been the most powerful anti-takeover device for Delaware targets and that it has been debated and challenged so extensively over the past ten years.¹⁰⁶

As noted in Part I.C, *Airgas* now seems to have removed most of the uncertainties concerning the validity of the device.¹⁰⁷ Does the very fact that Delaware companies can use staggered boards (and therefore make the reversal of the pro-target regime almost impossible) invalidate the *Unocal* passage stating that shareholders can always use “the powers of corporate democracy . . . to turn the board out”¹⁰⁸ and remove a defense? In other words, is the pro-management approach in Delaware de facto irreversible and therefore not a default?

103. *Id.* at 923.

104. See Lucian A. Bebchuk et al., *Staggered Boards and the Wealth of Shareholders: Evidence from Two Natural Experiments* (Harvard Law Sch., John M. Olin Ctr. Law, Econ. & Bus., Discussion Paper No. 697, 2011), available at http://www.law.harvard.edu/programs/olin_center/papers/pdf/Bebchuk_et%20al_697.pdf. But see Coffee & Palia, *supra* note 22, at 78-79 (citing studies that “support[] the view that staggered boards can provide stability and continuity that enhances shareholder value”).

105. By designating a staggered board “effective,” it means that the board’s staggered nature is hard-wired in the certificate of incorporation (and not in the bylaws) and cannot be declassified or “packed” (that is, increased in size to fill vacancies) by shareholders without approval from the board itself (all changes to the certificate of incorporation require approval by both the board and the shareholder) —given that the board is composed of incumbents, the chances of a hostile bidder declassifying an effective staggered board are minimal. Bebchuk, Coates & Subramanian, *supra* note 52, at 894; see DEL. CODE ANN. TIT. 8, § 242(b)(1)-(2) (2014). But see Subramanian, *supra* note 101, at 5-6 (proposing the conversion of effective staggered boards into ineffective staggered boards so that boards will have long-term continuity and shareholders will have the opportunity to decide on a hostile takeover bid in a “single, up-or-down referendum”) for a discussion of an alternative to declassifying effective staggered boards.

106. See *supra* note 101.

107. See *supra* note 54.

108. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 959 (Del. 1985).

Yes, in part. And no, in part.

In theory, after *Airgas*, Delaware targets can all be considered potentially takeover-proof, should they all avail themselves of a staggered board structure. For companies at the initial public offering (“IPO”) stage, this is clearly an option that issuer counsel should, and normally does, raise for management’s consideration.¹⁰⁹

However, things work quite differently for existing companies. Indeed, Delaware companies that have a staggered board in place amount to 45.8% in number and only 15.5% in terms of market capitalization.¹¹⁰ Furthermore, legal commentators have observed a trend of destaggering in the marketplace over the past decade.¹¹¹ Chances that existing companies adopt one are slim since implementing an effective staggered board, which can only be dismantled by a vote by both directors and shareholders, requires shareholder approval.¹¹² The very

109. See John C. Coates IV, *Explaining Variation in Takeover Defenses: Blame the Lawyers*, 89 CAL. L. REV. 1301, 1303-05 (2001).

110. See Table I, *infra* Part III.C.

111. See Tonello, *supra* note 43, at 10 n.10 and accompanying text; see also Subramanian, *supra* note 101, at 2, 9.

112. Adopting a staggered board can be unappealing to shareholders, so directors often do not even attempt to adopt it, as institutional investors would reject it. See Bebchuk, Coates & Subramanian, *supra* note 52, at 892. This however does not mean that existing corporations are never able to adopt one. Since 2007, twenty-one corporations have adopted a staggered board: CKRush, Inc., XPO Logistics, Inc., MeetMe, Inc., General Moly, Inc., VirnetX Holding Corp., Synutra International, Inc., BioDelivery Sciences International, Inc., Oculus Innovative Sciences, Inc., SunPower Corp., ReGen Biologics, Inc., Radient Pharmaceuticals Corp., INTL FCStone, Inc., NeoStem Inc., Earthstone Energy, Inc., Spectrum Brands, Inc., Isle of Capri Casinos, Inc., Bacterin International Holdings, Inc., Boulder Brands Inc., China Biologic Products, Inc., Nexstar Broadcasting Group, Inc., and Insys Therapeutics, Inc. See *Fact Set*, SHARKREPELLENT.NET (on file with author). The following table shows the yearly breakdown of how many corporations adopted a staggered board and how many corporations declassified their boards from 2007 through June 2013:

Year	Adoption of Classified Boards	Declassified Boards
2007	5	26
2008	4	32
2009	5	28
2010	1	40
2011	3	39
2012	1	46
2013 (through June 4)	2	33
Total	21	244

reason that poison pills were invented and became attractive was to avoid a shareholder vote to adopt the defense.¹¹³

Ultimately, whether a staggered board is in place and de facto allows a target to resist an unsolicited offer for at least thirteen months is much more important than who has the burden to reverse the default regime. The staggered board acts independently of the actual takeover law, which bans defenses only if they make a proxy contest realistically unattainable.¹¹⁴

Notably, in jurisdictions adopting the board neutrality rule, the presence of a staggered board does not have an impact on the reversibility of the default itself, given that shareholders, instead of casting their vote in an election contest, express their preference in favor of or against defensive measures, which in turn represents their say on the acquisition. Nonetheless, in such jurisdictions a staggered board could still impact a takeover contest by discouraging a prospective bidder from making an unsolicited offer for a company it will not be able to fully control following completion of the tender offer (assuming, of course, that directors cannot be removed in the absence of cause in such circumstances).¹¹⁵

b. Director Removability

The inability to remove directors other than for cause can deter hostile bidders under both regimes: in Delaware and in other pro-target jurisdictions, replacing the board to redeem the pill (or the relevant defense) would not be possible, and in a board neutrality regime, a winning bidder would have to negotiate with the current directors for

But see Advancing Annual Elections in the 2014 Proxy Season: Towards Declassification at 100 S&P 500 and Fortune 500 Companies, Shareholder Rights Project News Alert (Harvard Law Sch., Cambridge, Mass.), Dec. 4, 2013, at 1, available at http://srp.law.harvard.edu/newsletters/12-4-2013_SRP_newsletter.shtml (announcing that thirty-one shareholder proposals regarding board declassification were submitted to Fortune 500 and S&P 500 companies for a vote at their 2014 annual meetings and that seven companies have already agreed to declassify). *See also* Coffee & Palia, *supra* note 22, at 14 (noting that “[i]n 2000, 300 of the S&P 500 had staggered boards, but as of the end of 2013, only 60 did”).

113. *See supra* note 25, at 876-77.

114. *Versata Enters., Inc. v. Selectica, Inc.*, 5 A.3d 586, 601 (Del. 2010); *Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48, 113 (Del. Ch. 2011).

115. *See* CEPS REPORT, *supra* note 83, at 307 (“[S]taggered boards are not a feature of European company law.”).

their resignation or renewal.¹¹⁶ Once again, irrespective of the takeover regime, a corporate law collateral factor can play a crucial role in the outcome of a hostile tender offer (and therefore, from an ex ante perspective, in the likelihood that such an offer will ever be presented).

c. Shareholders' Ability to Call Special Meetings or Act by Written Consent

In Delaware, a shareholder vote on an acquisition might not occur until the first annual meeting of the target following the bid.¹¹⁷ This is the case for companies whose organizational documents neither empower shareholders to call special meetings¹¹⁸ nor allow them to act by written consent.¹¹⁹ In such circumstances, unless the acquisition is planned and launched sufficiently prior to the annual meeting of the target, a bidder will not be in a position to oust the incumbent board and have the pill redeemed. In other words, when bidders cannot call a special meeting or solicit stockholder consents, the Delaware regime implicitly gives a target's board an advantage—such an advantage runs

116. Jurisdictions adopting the board neutrality rule, such as the United Kingdom, and Italy, make it relatively easy to remove directors without cause (when removed without cause, directors typically get some form of monetary compensation but cannot get judicially reinstated). See Luca Enriques, Henry Hansmann & Reinier Kraakman, *The Basic Governance Structure: The Interests of Shareholders as a Class*, in REINIER R. KRAAKMAN ET AL., *THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH* 55, 61 (2d ed. 2009); Sofie Cools, *The Real Difference in Corporate Law Between the United States and Continental Europe: Distribution of Powers*, 30 DEL. J. CORP. L. 697, 750 (2005) (“[I]n most Continental European countries, a shareholder or group of shareholders can convene a meeting and then dismiss all directors by a mere majority vote.”) (footnote omitted) (emphasis omitted). *But see id.* at 739 (noting that removal is constrained in other countries in continental Europe such as Germany and Austria).

117. Cf. Robert B. Thompson & Paul H. Edelman, *Corporate Voting*, 62 VAND. L. REV. 129, 139 (2009) (noting that efforts by someone seeking control “to speed up the timetable are hindered by legal limits on non-managers’ ability to call a special meeting of shareholders or to act by written consent”).

118. In Delaware, stockholders can call special meetings only if the certificate of incorporation so provides. DEL. CODE ANN. TIT. 8, § 211(d) (2014) (“Special meetings of the stockholders may be called by the board of directors or by such person or persons as may be authorized by the certificate of incorporation or by the bylaws.”).

119. In Delaware, stockholder action may be taken by written consent in lieu of a meeting unless prohibited by the certificate of incorporation (either expressly or implicitly by requiring unanimous consent). *Id.* at § 228(a).

for a significant portion of each fiscal year and obviously vanishes the closer the company gets to the next annual meeting.

This is a problem peculiar to the Delaware regime as well as other jurisdictions adopting similar pro-target approaches, since in the United Kingdom system, as well as in any other regime adopting the board neutrality rule under the Directive, it will be the directors who actually call the meeting to obtain shareholder approval on the envisaged defenses.¹²⁰

At first glance, shareholders' inability to call special meetings or act by written consent may seem to be of limited impact: after all, a prospective bidder would just have to adequately plan and launch the bid at the right time, that is, in advance of the proxy season for an annual meeting. In other words, such corporations are in play only for certain periods of time during each fiscal year.

While this usually holds true in Delaware, in some circumstances the absence of special meetings and actions by written consent might have a deeper impact. Consider the following scenario: right after the time period for the annual meeting is over, a company announces a business combination with another company, which would neither trigger *Revlon* duties¹²¹ (and would therefore be subject to the more lenient *Unocal* and *Unitrin* standards),¹²² nor require a vote on the combination by the company's shareholders (think of a stock-for-stock exchange offer, as a result of which there is no change of control for *Revlon* purposes). In this hypothetical, not only would shareholders not be able to turn down the deal on a referendum basis, but also a potential competing bidder might never prevail in an auction, especially in the

120. Under the Directive, "Member States may adopt rules allowing a general meeting of shareholders to be called at short notice, provided that the meeting does not take place within two weeks of notification's being given." Council Directive 2004/25, art. 9, 2004 O.J. (L 142) 19 (EC).

121. Thus, the deal consideration must not be cash and the deal must be a combination "of equals" and not result in a change of control of the target company. Under *Paramount Commc'ns, Inc. v. QVC Network, Inc.*, 637 A.2d 34, 46-48 (Del. 1994), this would occur when the target company gets acquired by a company of a relatively similar size that does not have a controlling stockholder who would otherwise end up controlling the combined company: if the control of the target combined with the other entity would continue to stay fluid in the market, stockholders of the target would not face a loss in their voting rights and therefore *Revlon* would not apply. See *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986).

122. See *supra* notes 31-34 and accompanying text for a summary of the *Unocal* and *Unitrin* standards.

likely event that the target company insists on keeping its poison pill in place and the next annual meeting when the competing bidder can replace the board and get rid of the pill is too far away. In such a scenario, and in all other instances where a hostile bidder cannot quickly replace the board before it takes defensive actions that ultimately frustrate the attempted acquisition, the inability to call a special meeting and act by consent actually plays a crucial role and alters the outcome of what could have been a lively contest for the control of the company.

Consider that the Delaware regime stemming from the rulings in *Unocal*, *Unitrin*, *Versata*, and *Airgas*¹²³ allows directors to take certain defensive actions so long as such actions do not make a proxy fight realistically unattainable.¹²⁴ An analysis of a FactSet SharkRepellent database listing the universe of attempted hostile deals with a Delaware target from 2003 to June 2013¹²⁵ shows that at least in a couple of circumstances a bidder walked away from the acquisition without attempting a proxy fight after the target enacted defenses that chilled the bidder's interest.¹²⁶ While one could object to my main thesis that such deals – where targets successfully rebuff the bidder *without* having to resist any proxy fight – show how the Delaware regime does in fact

123. See *supra* notes 29-35.

124. See *Versata Enters., Inc. v. Selectica, Inc.*, 5 A.3d 586, 601 (Del. 2010); *Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48, 113 (Del. Ch. 2011).

125. *Fact Set*, SHARKREPELLENT.NET (June 7, 2013) (on file with author).

126. In the attempted acquisition of Exact Sciences, Corp. by Sequenom, Inc., valued at approximately \$40 million, Sequenom abandoned the acquisition without a proxy fight after the target sold its assets to Genzyme for \$24.5 million. Unexpectedly, based on the information that is publicly available, the latter's defensive transaction did not require a stockholders vote under Section 271 of the DGCL, and one of the conditions to closing was actually the receipt of legal opinion by Delaware counsel to that effect. See DEL. CODE ANN. TIT. 8, § 271 (2014); COLLABORATION, LICENSE AND PURCHASE AGREEMENT BETWEEN GENZYME CORPORATION AND EXACT SCIENCES CORPORATION 27-28 (2009), available at http://www.sec.gov/Archives/edgar/data/1124140/000110465909004443/a09-3865_1ex10d1.htm (Section 9.6). Further, nothing in the deal documentation suggests that the target was under *Revlon*. See Ryan McBride, *Exact Sciences Takes \$24.5M Genzyme Deal, Sequenom to Drop Buyout Offer*, XCONOMY.COM (Jan. 28, 2009), <http://www.xconomy.com/boston/2009/01/28/exact-sciences-takes-245m-genzyme-deal-sequenom-to-drop-buyout-offer/>.

In line with the pattern of abandoning an attempted transaction without a proxy fight, Stern Agee abandoned its attempted to acquire SWS Group after the target effected a defensive recapitalization that ultimately obtained stockholder approval. See SWS Group, Inc., Annual Report 34 (Form 10-K) (Sept. 7, 2012), available at <http://www.sec.gov/Archives/edgar/data/878520/000119312512383471/d371938d10k.htm>.

favor targets significantly, I argue that they do not weaken my arguments. For starters, the SWS Group deal *did* entail a stockholder vote that approved the defensive recapitalization and de facto voted against the offer on the table.¹²⁷ A bidder confident to win would have had time to mount a proxy fight to replace the directors and reject the defensive recapitalization. The fact that it did not start a proxy fight probably resulted from the ownership structure of the target: if the target was able to accumulate the votes to approve the recapitalization, the composition of its stockholder base must have dissuaded the bidder from launching the proxy contest in the first place. In other words, *Unocal* (and its progeny) alone played no role. With respect to the attempted acquisition of Exact Sciences, leaving aside that it is not quite clear why neither *Revlon* nor a Section 271 vote were triggered, my thesis is confirmed *because corporate law collateral factors were actually at work*. The bidder was in no position to remove the target's directors either by calling a special meeting or soliciting written consents.¹²⁸ Even the hotly contested and ultimately failed attempt to acquire Allergan by Valeant and Pershing Square of 2014 fits with the analysis I present in this Article.¹²⁹ Indeed, the bidder(s) had managed to call a special meeting to replace the board and redeem Allergan's pill: nobody knows how, without the counter offer by Actavis, things would have played out in such a meeting. True, the pill helped Allergan in delaying the Valeant/Pershing Square takeover. However, launching the offer so much earlier than the meeting ultimately gave Allergan enough time to organize and find an alternative, value maximizing transaction with

127. See *supra* note 126.

128. See Exact Corp., Sixth Amended and Restated Articles of Incorporation of Exact Corporation 3 (1995), available at http://www.sec.gov/Archives/edgar/data/1124140/000091205700046284/a2027577zex-3_3.txt; Exact Corp., Amended and Restated By-Laws of Exact Corporation 5-7, available at http://www.sec.gov/Archives/edgar/data/1124140/000091205700046284/a2027577zex-3_4.txt.

129. As I write, the Allergan saga has just entered an entirely new (and possibly final) chapter with the announcement of the \$66 billion white knight transaction with Actavis on November 16, 2014, which first bidder Pershing Square, with expected paper gains of \$2.3 billion, has supported, therefore putting an end to its acrimonious contest with the target. See *Ackman supports Allergan's \$66 billion sale to Actavis*, REUTERS, Nov. 18, 2014, available at <http://www.reuters.com/article/2014/11/18/us-allergan-m-a-ackman-idUSKCN0J21X920141118>. For an earlier and critical account of the Allergan attempted hostile takeover, see Coffee & Palia, *supra* note 22, at 41-45.

Actavis.¹³⁰ In other words, it was the corporate law collateral factor (that is, the inability to promptly call a shareholder meeting) and not *Unocal* alone that thwarted the takeover.¹³¹

Finally, the inability for shareholders to call special meetings (or some material constraints to a call, such as requiring the meeting be called by shareholders owning a significant stake)¹³² or act by written consent might be a much more relevant barrier in pro-target jurisdictions where, unlike Delaware, directors are not up for re-election every year: in such circumstances, their removability (and the elimination of takeover defenses) is significantly limited. In other words, the inability to call special meetings ceases to be a corporate law collateral factor of a mild nature when coupled with a regime that contemplates director terms longer than one year.

d. Supermajority Rules

Both the Delaware and the United Kingdom systems contemplate shareholder voting as a way to establish whether a hostile acquisition attempt should go through. In general, when a group of individuals coalesces through a voting mechanism, the underlying assumption is that “the majority opinion expresses the ‘group preference’, *i.e.*, the optimal choice for the group as a whole.”¹³³ As Zohar Goshen states, “when a large number of voters attempt to ‘guess’ at the best choice, the ‘guess’ of the largest group will, statistically speaking, be the ‘correct’

130. Note incidentally that, given the combination with Actavis by way of a merger, Allergan’s shareholders will get to vote on the acquisition (only this time under Section 251 of the DGCL).

131. One could also speculate (without obviously ever being able to prove it) that, without the time Allergan bought with the pill and its cumbersome rules for calling a special meeting, a transaction with such a high premium like the one with Actavis would have been more difficult to secure: it is ironic that possibly because of the pill Pershing Square is now able to walk netting a staggering \$2.3 billion paper gain as a consolation prize.

132. On both sides of the Atlantic, the statutory right to convene special meetings is generally subject to certain fine-tuning of the organizational documents, and it is seldom an all-or-nothing issue. Jurisdictions generally require that shareholders must represent a minimum threshold of shareholder capital to request a special meeting. *See* Cools, *supra* note 116, at 731-33 (discussing Delaware, Belgium, and France).

133. Goshen, *supra* note 100, at 399.

one.”¹³⁴ Indeed, “[t]here is no reason to suppose *a priori* that the minority’s rejection of a proposed transaction is preferable when the majority of the group’s members believe the transaction to be worthwhile.”¹³⁵

On the contrary, supermajority provisions (e.g., requiring a two-thirds vote) do favor minorities over majorities in all instances in which a minority coalition is able to block a resolution that a simple majority would otherwise approve (i.e., 66.6% > majority vote obtained at the actual meeting > 50%).¹³⁶

In the takeover world, this means that when a supermajority is necessary to pass a resolution to reverse the regime, those whose interests are protected by the regime have a significant advantage over those who seek to reverse it.

Some jurisdictions imposing the board neutrality rule do require that certain defensive actions be approved by a supermajority. For instance, to pass certain defenses Italian companies need an approval of two-thirds of the shares present at the meeting (meaning it will be enough for a bidder to form a one-third plus one share vetoing minority to block the defense).¹³⁷ A study commissioned by the European Commission sampled 464 listed companies among sixteen Member States and found that “[a]ll companies in the sample are subject to supermajority provisions for some resolutions at extraordinary general meetings, based on national regulation.”¹³⁸ Furthermore, European companies are generally free to raise, by private ordering, the required

134. Zohar Goshen, *Voting and the Economics of Corporate Self-Dealing: Theory Meets Reality* 7, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=229273

135. *Id.* at 8 (noting that “it is also in the minority’s interest, *ex ante*, that the majority view prevails”).

136. For example, in early 2009, after Biotechnology Value Fund attempted a tender offer and launched a proxy fight to acquire Avigen. The bidder called a special meeting to replace existing directors with a four-person slate. Although the bidder/insurgent obtained 58% of the vote, the acquisition fell through because a supermajority of 66.67% was necessary to remove directors. *See Biotech Firm to Liquidate Under Investor’s Pressure*, DEALBOOK (Mar. 30, 2009, 6:02 AM), http://dealbook.nytimes.com/2009/03/30/biotech-firm-to-liquidate-under-investors-pressure/?_r=0.

137. *See* Codice civile, art. 2368-69 (It.).

138. EUROPEAN COMMISSION, REPORT ON THE PROPORTIONALITY PRINCIPLE IN THE EUROPEAN UNION 23 (2006), available at http://ec.europa.eu/internal_market/company/docs/shareholders/study/final_report_en.pdf.

majorities to pass certain actions.¹³⁹ By doing so they can make it much harder to pass such actions during takeover attempts. Arguably, this is less of a risk for companies subject to the board neutrality rule than for companies that are not, given that incumbents in board neutrality rule companies can anticipate that a supermajority requirement would hinder any defense against a hostile takeover offer).

In the board neutrality regime, when a supermajority is necessary to pass a resolution, those whom the default favors (that is, bidders) are advantaged: to win the vote, they will simply need to accumulate a block sufficient to ensure the defensive measure will not be approved by the required supermajority. Note that none of these supermajority rules are typically part of the actual takeover regulation; they are general requirements under applicable corporate laws for the approval of resolutions that entail an amendment of the articles of association — regardless of whether their purpose is defensive. In sum, combined with a board neutrality regime, supermajority requirements represent a corporate law collateral factor that can alter the reversibility of the takeover regime and favor bidders.

Similarly, in the opposite scenario, any supermajority requirement for the election and/or removal of directors of a Delaware company makes it more difficult for a bidder to replace the board and redeem the pill. From a practical standpoint, the election of directors is not a problem prospective bidders face, because there are no Delaware companies of which I am aware that require a supermajority to elect directors.¹⁴⁰ However, there are several companies that require supermajorities to remove directors, whether or not for cause.¹⁴¹

Because reversing the default is harder when a supermajority vote is necessary to pass the relevant resolution, a jurisdiction's default favors one side of the takeover battle. This is especially true in circumstances where those who oppose the default regime are only able to accumulate a simple majority.

139. *Id.* at 21 (“All countries, except France and Ireland (where the situation is unclear) allow companies to introduce supermajority provisions in their by-laws[.]”) (footnote omitted).

140. The reasoning is intuitive: having to obtain a supermajority to pass resolutions on a regular basis, such as those to elect directors, would be very disruptive for a company. As an example, companies with low turnouts at annual meetings would struggle to get the required votes to appoint directors.

141. In particular, there are 642 Delaware companies (27.4% of all Delaware public corporations, and 14.7% in terms of market capitalization) that require a supermajority vote to remove directors. *See infra* Part III.C.

e. Rules on Proxy Contests

In the presence of barriers to proxy contests, it will be more difficult for shareholders to reverse the regime. If a proxy regime is incumbent-friendly, for instance, by requiring a shareholder to hold a minimum percentage of shares over a period of time before mounting a proxy contest,¹⁴² it will be more difficult to change the status quo, and the default regime on takeover defenses will have a significant impact on the outcome of the contest.¹⁴³ While one would expect that proxy rules would naturally strive to set a neutral balance between incumbents and insurgents, in the world of hostile acquisitions biased proxy rules end up favoring one side of the control contest. Depending on where the takeover default regime lies, such rules can impact the ultimate outcome of the acquisition: in jurisdictions following the Delaware approach,

142. This might disqualify certain bidders from soliciting proxies.

143. I do not believe that pro-incumbent rules on the reimbursement of proxy expenses necessarily fit into this category and represent a single factor that can discourage or prevent a proxy fight in the broader context of a hostile deal. For instance, the Froessell Rule—followed in both New York and Delaware—allows incumbents to be reimbursed for proxy contest expenses regardless of the outcome when (i) the proxy contest involves questions of policy (as opposed to purely personal reasons), (ii) the expenses are reasonable and necessary for informing the corporation's shareholders of the board's policy stance, and (iii) the challengers' potential for reimbursement is significantly limited. *See, e.g.*, *Rosenfeld v. Fairchild Engine & Airplane Co.*, 128 N.E.2d 291, 293 (N.Y. 1955) (N.Y.); *Hall v. Trans-Lux Daylight Picture Screen Corp.*, 171 A. 226, 227 (Del. Ch. 1934) (Del.); *see also* *CA, Inc., v. AFSCME Emps. Pension Plan*, 953 A.2d 227, 237-39 (Del. 2008) (declaring as violative of Delaware law a shareholder-proposed bylaw that would reimburse challengers in a proxy contest); *Bebchuk & Kahan, supra* note 11, at 1106-08. *But see* DEL. CODE ANN. TIT. 8, § 113 (2014) (allowing corporations to adopt bylaws that provide reimbursement to challengers in a proxy contest). I do not believe reimbursement rules are that significant in the context of acquisitions, especially if the target is of a non-trivial monetary size, since the cost of the proxy fight would represent one of many other costs that a bidder would likely be prepared to incur. *See supra* note 92. By way of illustration, the most expensive proxy fights from 2008 to 2012 cost anywhere from \$9 million to \$22 million with incumbent boards spending significantly more than challenger dissidents. During that same time, proxy solicitor fees ranged from \$1 million to \$2.5 million, again with incumbents significantly outspending challengers. *See* Adam Kommel, *Proxy Fight Fees and Costs Now Collected by SharkRepellent: Mackenzie Partners and Carl Icahn Involved in Largest Fights*, SHARKREPELLENT.NET (Feb. 20, 2013), https://www.sharkrepellent.net/request?an=dt.getPage&st=undefined&pg=/pub/rs_20130220.html&Proxy_fight_fees_and_costs_now_collected_by_SharkRepellent&rnd=169632.

bidders will find it more difficult to appoint new directors and get rid of anti-takeover devices; conversely, in jurisdictions following the U.K. system, those who oppose the bid and seek to authorize defenses will struggle to get such measures approved at a shareholders meeting.¹⁴⁴

f. Shareholders' Conflict of Interest

Rules governing conflict of interest by shareholders also play an important role. In theory, in order to have two regimes that are perfectly indifferent to shareholders, each shareholder resolution that reverses the default regime set by the legislature should not be affected by the conflict of interest of one or more shareholders. In the absence of a "sincere"¹⁴⁵ vote, where the outcome of the vote can easily be altered by

144. One could also hypothesize that if proxy rules are so significantly biased toward either side, the anti-takeover regime ultimately might not matter. In other words, all else being neutral (with no supermajority requirements, staggered board, or other corporate law collateral factors playing a role) and depending on the actual ownership structure of the target corporation in question, if proxy rules are significantly biased in favor of incumbents or insurgents, they can be much more relevant than the actual anti-takeover default regime in determining the outcome of the acquisition. Consequently, if both the anti-takeover regime and the proxy rules favor targets and incumbents, it will be very difficult for bidders to reverse the regime. Note that the ultimate outcome of the control contest should not change if the anti-takeover default regime is pro-shareholder *and* the proxy regime is unbalanced and biased for incumbents because an unbalanced, pro-incumbent proxy regime would probably help shareholders that hold a control block approve a defense to the bid. In contrast, in the unlikely case of a pro-target, anti-takeover default regime where the proxy rules significantly favor insurgents, bidders would have an easy time reversing the default. This might be considered as potentially detrimental as entrenchment because it could lead to too many acquisitions where bidders could exploit investors by paying insufficient premiums. Obviously, if the anti-takeover default regime were pro-shareholder, a pro-insurgent proxy regime would exacerbate such a risk.

145. See Goshen, *supra* note 99, at 815-16. The importance of sincere voting is intuitive, and is echoed in some case law (but not case law dealing specifically with hostile deals). For example, consider the emphasis on the need for "majority of the minority" voting and its effectiveness that the Delaware Chancery Court expressed in *In re Pure Resources, Inc. Shareholders Litigation*, 808 A.2d 421 (Del. Ch. 2002) (involving an attempt by a controlling shareholder to make a tender offer to purchase remaining shares of a corporation through an approval process that included a majority of the minority provision that did not perfectly remove all affiliated shareholders—including the board members—from such consideration). Without an effective majority of the minority provision, a shareholder vote alone is considered useless. Obviously, this is more so the case for entire fairness type of deals given the presence of a controlling stockholder; yet things are not conceptually that different in a hostile deal

a conflicted vote, setting the default rule in one direction or the other can impact the outcome of the acquisition.

For example, let us assume that: (i) target company X is incorporated in a jurisdiction embracing a pro-target rule comparable to Delaware's and is subject to an unsolicited tender offer; (ii) both management and bidder own 14.9% of the stock of company X; (iii) shareholders are called to vote to oust the board so that the pill can be redeemed; (iv) the tender offer has a sizable premium and is thus favored by a majority of disinterested investors; and (v) the given jurisdiction is capable of policing conflicted voting, say, there is a majority of the minority rule in place and therefore shares held by the incumbents (14.9% of the stock) and insurgents (14.9% of the stock) will not be counted (or general principles on conflicted voting can otherwise ensure that same result). Under these circumstances, given (iv), target shareholders would be able to replace the board allowing the acquisition to go through.

The outcome would not change if target company X were incorporated in a jurisdiction embracing the board neutrality rule. Assuming shareholders voted to approve some takeover defenses proposed by the board, given again (iv), the same target shareholders who were in favor to replace the board and have the pill redeemed under the first example would vote against the board proposal to erect defenses and the acquisition would still go through.

However, the outcome would change (and play out differently in the two jurisdictions depending on the default regime), if the given jurisdiction were not effective in policing conflicted voting. For example, a given jurisdiction might prevent the insurgents but not the

scenario with both management and bidder likely having accumulated significant stakes in the corporation. Surprisingly, it appears that the Delaware judiciary has been silent on conflicts of interests in connection with proxy fights to replace a board and redeem the pill. See Leonard Chazen, *Did the Dell Minority-of-the-Majority Clause Go Too Far?*, LAW360 (July 22, 2013, 2:29 PM), <http://www.law360.com/articles/459110> (warning on risks of non-consummation when majority-of-the-minority clauses are drafted in an over-inclusive manner: “[t]he type of majority-of-minority clause used in the Dell agreement, which requires approval by a majority of the outstanding unaffiliated shares, instead of a majority of those voting on the transaction, makes the failure to cast a vote the equivalent of a vote against the deal.”); Sharon Terlep, *Dell Buyout Group Calls for Change in Voting Rules*, WALL ST. J. (July 24, 2013), <http://online.wsj.com/article/SB10001424127887323610704578625550322614778.htm> 1.

incumbents from voting on the actual resolution—or vice versa. Assuming that, under the given rules on conflict of interest, insurgents cannot vote but incumbents can, under the Delaware regime, this means that incumbents will have a better chance at resisting the hostile attempt to replace them in the proxy fight; similarly, in a system adopting the board neutrality rule, directors will find it easier to have enough votes to pass the resolution authorizing the defenses. Under both systems, incumbent-friendly rules on shareholder conflict of interest might well alter the outcome of the acquisition. Conversely, if the given rules allow insurgents but not incumbents to vote, the acquisition would have a higher chance to go through under both the Delaware and the United Kingdom regimes, and therefore the outcome would be no different than if effective rules existed. Note, however, that in the above fact pattern shareholders wanted the acquisition to succeed: in the opposite case of a low-ball offer that shareholders do not think beneficial, insurgent-friendly conflict of interest rules would tilt the balance in the insurgents' favor toward a replacement of the incumbent board (in Delaware) or a rejection of the defenses proposed by the board (in the United Kingdom) that would be at odds with shareholder preferences. Once again, rules external to the takeover regime itself would be determinative of the outcome of the acquisition.

2. Structural vs. Transactional Defenses and the Two Default Regimes

Different default regimes may lead to different outcomes in terms of the actual defensive measures that emerge in a given market. Some believe that the Delaware system offers more fertile ground for so-called structural defenses.¹⁴⁶ A structural defense, like the poison pill, consists of a “legal mechanism . . . often adopted in advance of a bid, designed to deter or impede bids *without having a financial or operational effect on the target.*”¹⁴⁷

The pill is a mere deterrent that does not trigger substantial costs for the target – it only signals a “no” to a potential bidder, unless the board decides to redeem it or the board itself is replaced by the bidder through a proxy contest. Other defensive tactics can be less popular among shareholders, because they commit target companies to certain risks, including taking on more debt or making a significant acquisition, which can have negative consequences on the stock price.

146. Kahan & Rock, *supra* note 25, at 909.

147. Coates, *supra* note 109, at 1306 n.17 (emphasis added).

It is common wisdom that European companies cannot adopt poison pills, and indeed they do not adopt them.¹⁴⁸ Authors suggest that one of the main features that make a poison pill a viable defensive measure is that the pill does not require a shareholder resolution, which would delay a prompt and effective adoption of the defensive device.¹⁴⁹ Furthermore, the possibility that a widely held company's shareholders would approve the adoption of a poison pill is considered remote.¹⁵⁰

A pro-shareholder default would seem to limit structural defenses¹⁵¹ and de facto imply that companies would have to rely on transactional defenses only, which consist of a smaller and less effective arsenal, since they require taking operational actions that might end up costing money to the company, with a negative effect on the share price. In such cases, shareholders might perceive the bid as the lesser of two evils.¹⁵²

148. Guido Ferrarini, *Corporate Ownership and Control: Law Reform and the Contestability of Corporate Control* at the Conference on Company Law Reform in OECD Countries 14 (Dec. 7, 2000), available at <http://www.oecd.org/daf/ca/corporategovernanceprinciples/1931676.pdf> ("Poison pills are not used and would probably violate either corporate law principles or stock exchange regulations and companies' best practices.") (footnote omitted); Gordon, *supra* note 24, at 549-50. See also CEPS REPORT, *supra* note 83, at 307 (citing the findings, limited to the United Kingdom, Germany, and Italy by Gerner-Beurle, Kershaw & Solinas, *supra* note 86).

149. See, e.g., Kahan & Rock, *supra* note 25, at 909.

150. Coates, *supra* note 109, at 1306-07 ("[S]hareholder approval . . . has not generally been forthcoming for defenses since institutional shareholders organized in the late 1980s. . . . [E]ven when a bid is not on the table, shareholders have been unwilling to approve defenses."); Gordon, *supra* note 24, at 551 n.23. See also Lucian A. Bebchuk, *Why Firms Adopt Antitakeover Arrangements*, 152 U. PA. L. REV. 713, 715 n.4, 723-24 (2003) (concerning shareholder approval of other defensive arrangements).

151. In the context of a proxy fight in connection with an attempted takeover of a Delaware company, when deciding to cast their vote for the insurgents or the incumbents, shareholders are essentially voting for or against the bid itself (they compare the bid price with the expected value of the target should it remain independent). They have a simple binary choice: voting to replace the current board means they want the bid to succeed; voting to maintain the current board expresses their preference to keep the pill in place and maintain the target's independence.

152. For instance, assume that there is a \$48 per share unsolicited bid on the table (with, say, a 20% premium over a pre-bid market price of \$40), but the market attaches an expected price target of \$60 per share if the target stays independent. In such a scenario, shareholders of a Delaware company would likely vote for the incumbents' slate to maintain the pill in place and the company's independence. In a jurisdiction that does not contemplate structural defenses, the company would have to adopt transactional defenses. If the market perception of such defenses is negative (assuming

However, the unavailability of structural defenses under a pro-shareholder regime should not be a reason to endorse a pro-target policy approach. The absence of poison pills and of similar mechanisms in jurisdictions adopting a pro-shareholder approach has nothing to do with the anti-takeover default regime itself. Rather, it is the inflexibility of its corporate law rules and principles that does not allow adopting structural or similar defenses: that is, giving shareholders the ability to decide between the bid and the hypothetical value of the independent target. In theory, if a jurisdiction's corporate law permitted resolutions that, if approved, would ban a bidder from completing the transaction without the need for the target to take any further action, even the board neutrality rule would permit shareholders to decide whether or not they want the bid to succeed.¹⁵³

So it is not the takeover regime's effect on *who* is to adopt anti-takeover defenses that is the crucial point, but rather *what* defenses are available. The issue of the spectrum of available defenses to say "no" effectively (that is, without disrupting the operations of the company) has greater relevance than the much-debated issue of what is the best-suited corporate body to have a final say on takeover defenses.¹⁵⁴ It is

that their adoption is expected to drag the value down to below \$40), shareholders would likely reject them, thus allowing the bid to succeed—note that they would let the bid go through even if the value of the target as an independent company would have been much greater (\$60 as opposed to \$48 per share). The absence of structural defenses may lead to inefficient outcomes whenever incumbents fail to convince shareholders that after the adoption of the defense the target will be worth more than what the bidder is offering. See Gatti, *supra* note 86, at 106-07.

153. This is precisely why, rather than the default regime itself, it is the actual availability of structural defenses that acts as a strong disincentive to creeping acquisitions, that is, acquisitions made through open purchases in the market or other street sweeps techniques, which allow a person to gain de facto control without actually ever launching a tender offer. If structural defenses were available in jurisdictions adopting the board neutrality rule, a prospective acquirer of de facto control would likely be barred from accumulating a very significant foothold without actually triggering the structural defensive mechanism. For example, poison pills have triggering thresholds ranging from 5% to 20% of a corporation's voting stock. See *supra* note 23 and accompanying text.

154. If the spectrum is very limited, then a pro-target default would perform better. Nevertheless, this has nothing to do with the default regime itself, especially if the regime is silent on the point. I tend to agree with Professor Luca Enriques, of the University of Oxford faculty of law, as he pointed out to me when commenting on an early draft of this article, that one should not necessarily ascribe the unavailability of structural defenses to corporate law. According to Enriques, the unavailability may be considered a product of what he labels as "negative takeover law," that is, the lack of a

not really about who calls the shots, but what type of shots a company can use.

3. *Summary and Preliminary Remarks*

In Part III.A, I have observed that in the abstract the Delaware regime coupling poison pills and proxy fights and the British board neutrality rule can lead to the same results and therefore can be considered as simple default regimes that shareholders can reverse (specifically, if shareholders want the acquisition to succeed in Delaware and fail in the United Kingdom). If shareholders can ultimately decide, those takeover regimes can be considered neutral if not immaterial.

However, as Part III.B has shown, there exist corporate law collateral factors that can tip the scales in favor of the default regime, including: the election and voting fronts, staggered boards, limitations to director removability, shareholders' inability to call special meetings or to act by written consent, supermajority provisions, unbalanced proxy rules, and ineffective rules policing shareholders' conflict of interest.

The question then becomes: How relevant are these corporate law collateral factors?

There are two possibilities here: either (1) their impact is minimal or not material, and one could conclude that the over thirty year debate on the optimal allocation of power between shareholders and directors is dealing with a secondary issue *or*, (2) if their impact actually turns out to be of some relevance, the debate has then been focusing too much on the takeover regime and, with some exceptions, too little on these corporate law collateral factors that act as barriers to the reversibility of the default.

takeover rule (either implicit or explicit) that can guarantee an effective veto on takeovers. The lack of such a rule is in my view what actually makes corporate law relevant on this front. This is why I argue that takeover law and policy should address such issues.

C. PRACTICAL RELEVANCE OF THE CORPORATE LAW COLLATERAL
FACTORS THAT ALTER THE DELAWARE REGIME

Part III.C analyzes a sample of 2417 Delaware public corporations from a FactSet SharkRepellent database,¹⁵⁵ which represents the universe of Delaware public corporations as of August 28, 2013.

Out of that total, there are 679 corporations where none of the following corporate law collateral factors are at work: staggered board, supermajority to remove directors, inability for shareholders to call special meetings or to act by written consent, and no director removability in absence of cause. These 679 corporations amount to 28.1% of the total number of Delaware public corporations and 59.3% in terms of market capitalization. Leaving aside other factors such as ownership structure, and assuming a neutral impact of proxy rules and conflict of interest rules and that no significant corporate law collateral factors are also at work, these corporations, totaling over half the market capitalization of Delaware companies, differ very little from their United Kingdom peers in terms of how takeover proof they are from a purely legal standpoint. The fact that these corporations can adopt and/or keep a pill in place should not matter if a hostile tender offer is launched and shareholders are requested to cast their vote to approve or reject the acquisition.¹⁵⁶

155. August 2013 FactSet SharkRepellent Delaware Database (on file with author).

156. The following table selects some data included in the Takeover Defense Trend Analysis Snapshots for 2008 and 2013 provided by FactSet SharkRepellent (on file with author), which, unlike the August 2013 FactSet SharkRepellent Delaware Database that only includes data from corporations incorporated in Delaware, aggregates data for all U.S. corporations. In looking at the Takeover Defense Trend Snapshots for 2008 and 2013, one can observe a slight decrease in the number of companies using corporate law collateral factors to make themselves takeover proof.

	2008	2013
Number of Corporations	3869	3768
Staggered Board	50.50%	43.52%
Shareholders cannot call special meetings	53.09%	50.53%
Shareholders cannot act by written consent	69.73%	69.13%
Directors removed only for cause	47.97%	46.36%
Supermajority required for director removal	31.84%	31.40%

Turning to Delaware corporations, where corporate law collateral factors are at work, the August 2013 FactSet SharkRepellent Delaware Database reveals the following:

(i) staggered boards—there are 1106 corporations with a staggered board in place, which account for 45.8% of the total corporations and 15.5% in terms of market capitalization;

(ii) special meetings/action by written consent—there are 1220 corporations in which shareholders can neither call special meetings nor act by written consent, which account for 50.5% of the total corporations and 31.5% in terms of market capitalization;

(iii) supermajority to remove directors—there are 655 corporations in which shareholders need more than a simple majority to remove directors, which account for 27.1% of the total and 14.7% in terms of market capitalization, which, to avoid overlaps, is appropriate to isolate as follows:

(a) if we exclude corporations with staggered boards, we are left with 200 corporations, which account for 8.3% of the total and 8.8% in terms of market capitalization,

(b) if we exclude corporations in which shareholders can neither call special meetings nor act by written consent, we are left with 154 corporations, which account for 6.4% of the total and 2.2% in terms of market capitalization, and

(c) if we exclude corporations with staggered boards *and* in which shareholders can neither call special meetings nor act by written consent, we are left with sixty-nine corporations, which account for 2.9% of the total and 1.2% in terms of market capitalization; and

(iv) director removability only for cause—there are 1149 corporations in which directors cannot be removed without cause, which account for 47.5% of the total and 23.7% in terms of market capitalization, which, to avoid overlaps, is appropriate to isolate as follows:

(a) if we exclude corporations with staggered boards, we are left with 231 corporations, which account for 9.6% of the total and 10.1% in terms of market capitalization,

(b) if we exclude corporations in which shareholders can neither call special meetings nor act by written consent, we are left with 323 corporations, which account for 13.4% of the total and 7.6% in terms of market capitalization, and

(c) if we exclude corporations with staggered boards *and* in which shareholders can neither call special meetings nor act by written

consent, we are left with 101 corporations, which account for 4.2% of the total and 4.4% in terms of market capitalization.

Table I breaks down all of the data collected.

Table I Corporate Law Collateral Factors at Work with Delaware Public Corporations (August 2013 FactSet Delaware Database)

Corporate Law Collateral Factor	Number	Percent	Amount Market Cap (Millions)	Percent Market Cap
Staggered board	1106	45.8%	\$1,794,237	15.5%
Shareholders can neither call special meeting nor act by written consent	1220	50.5%	\$3,649,770	31.5%
Supermajority required to remove directors:	655	27.1%	\$1,707,478	14.7%
a. Without a staggered board	200	8.3%	\$1,015,577	8.8%
b. Without limitations on shareholders' ability to call special meetings/act by written consent	154	6.4%	\$255,918	2.2%
c. Without either staggered board and limitations on shareholders' ability to call special meetings/act by consent	69	2.9%	\$133,746	1.2%
Directors can only be removed for cause:	1149	47.5%	\$2,742,295	23.7%
a. Without a staggered board	231	9.6%	\$1,174,426	10.1%
b. Without limitations on shareholders' ability to call special meetings/act by consent	323	13.4%	\$882,263	7.6%

Corporate Law Collateral Factor	Number	Percent	Amount Market Cap (Millions)	Percent Market Cap
c. Without either staggered board and limitations on shareholders' ability to call special meetings/act by consent	101	4.2%	\$510,156	4.4%
Corporations without any of the foregoing corporate law collateral factors	679	28.1%	\$6,862,069	59.3%
Corporations without staggered board, supermajority to remove directors and director removability only for cause	935	38.7%	\$7,929,400	68.5%
Total Corporations	2417	100%	\$11,580,189	100%

In looking at the data, one might notice that the relatively high percentage of Delaware corporations with a staggered board (45.8%) is mainly composed of small-to-mid caps, since in terms of market capitalization the percentage is relatively small (15.5%): it is no surprise that small-to-mid caps are easier targets to conquer in a hostile deal (easier both in terms of the amount of investment required and in terms of the PR complexity of winning larger corporations).

Corporations in which a supermajority is required to remove directors and win a proxy fight are a little over one quarter of all the corporations (27.1%) and a smaller portion from a market capitalization standpoint (14.7%). There are 200 corporations that do not have a staggered board but do require a supermajority to remove directors, which is 8.3% of all corporations and 8.8% in terms of market capitalization. This finding is relevant, as supermajorities have been neglected by the scholarship that focused on staggered boards, yet these

companies have enhanced defenses that make the reverse of the pro-target default quite problematic as shown earlier on in this article.¹⁵⁷

With regard to stockholders' ability to call special meetings or act by written consent, for 50.5% of corporations (31.5% in terms of market capitalization), hostile bidders are de facto compelled to wait for the next annual meeting to have a vote on the acquisition. As noted earlier in Part III.B.1.a, the impact of this corporate law collateral factor is generally not very significant, as it can be dealt with through adequate pre-planning. If we ignore this factor and consider only corporations without a staggered board, with no supermajority required to remove directors and in which directors can be removed without cause (that is, corporations where all strong corporate law collateral factors are absent), we have a total of 935 corporations, which represent 38.7% of the sample (68.5% in terms of market capitalization). This means that corporations totaling 68.5% of the aggregate market capitalization of Delaware public corporations do not have significant corporate law collateral factors at work that make a reversal of the pro-target default regime particularly hard.¹⁵⁸

In other words, in terms of market capitalization, approximately 70% of the value of Delaware companies is *not* subject to stringent defenses against hostile takeovers irrespective of whether they have adopted a poison pill.

IV. AN ASSESSMENT OF THE TWO "DEFAULT" REGIMES

Part III showed that, assuming the absence of what we called corporate law collateral factors, the difference between the Delaware and U.K. anti-takeover regimes is negligible. Part III.C showed that 28.1% in terms of number and 59.3% in terms of capitalization in a sample of 2417 Delaware public corporations are not affected by corporate law collateral factors (the percentages rise to 38.7% and 68.5%, respectively, if we do not consider shareholders' inability to call special meetings or to act by written consent, which are admittedly the least pervasive of those factors). It is no surprise that in Delaware the

157. See *supra* Part III.B.1.d.

158. Except that in some of these corporations, hostile bidders would need to plan their bids around the corporation's annual meeting in order to be able to replace the directors and redeem the pill.

real heat of the legal battle shifted from strict takeover law to one of the main corporate law collateral factors we described—staggered boards.¹⁵⁹

Assuming the presence of one or more of those corporate law collateral factors, and therefore assuming the takeover regime does ultimately matter, Part IV seeks to determine which regime is preferable in the abstract to preserve shareholders' power to determine the outcome of an acquisition, which in turn depends on what corporate law collateral factors are at work and how they interact with the regime.¹⁶⁰

To be sure, some problems are common to both regimes.

First, supermajority provisions alter the reversibility of the default. In a pro-target regime, this means more entrenchment, since a simple majority of the share capital would not have the ability to remove the board to eliminate the defenses in place. In a pro-shareholder regime, a supermajority provision implies less likelihood that defenses would ever be approved, which might possibly result in an excess of value-decreasing acquisitions that cannot be screened out by a shareholder vote.

Second, proxy rules can play a crucial role and, as noted earlier in Part III.B.1.c, if they are significantly biased for either side, the anti-takeover regime will ultimately not matter. In other words, if all else is equal (that is, with no supermajority requirements, staggered board or other corporate law collateral factors at work), if proxy rules are so significantly biased in favor of incumbents or insurgents that they might well be more relevant than the actual anti-takeover default regime in determining the ultimate outcome of the acquisition.

159. See *supra* note 54.

160. This Article briefly discusses (*infra* Part IV.C) whether it is preferable for the takeover regime to be mandatory in nature, meaning set by the legislature *yet* subject to the possibility for shareholders to reverse it during an actual bid, or optional in nature, allowing corporations to choose whatever regime they want, subject to certain procedures regarding midstream changes. See *infra* Part IV.C; see also Enriques, Gilson & Paces, *supra* note 92, at 12-14. As I will point out *infra* Part IV.C, I tend to agree from a policy standpoint that “individual companies should be able to decide ‘who decides[]’” (whether a hostile takeover goes forward). However, it is essential to remember that if what companies are determining is just the “who decides” question, while neglecting the corporate law collateral factors, the benefits of letting companies decide would be limited. See *infra* Part IV.C; see also Enriques, Gilson & Paces, *supra* note 92, at 4-5.

Third, ineffective rules policing conflict of interest might increase the chances of success of either the directors or the bidder depending on whether those rules are incumbent- or insurgent-friendly, respectively.

A. THE PRO-TARGET DEFAULT REGIME IN LIGHT OF THE CORPORATE LAW COLLATERAL FACTORS

When a jurisdiction's corporate law is flexible enough to permit structural defenses, a pro-target default regime allows shareholders to decide whether or not the bid should succeed without the need to take any operational action that might not be an effective response and/or might waste value.¹⁶¹ Additionally, even if the Delaware approach does not insulate directors from market forces, it gives them the psychological comfort that they will be well positioned to negotiate with the bidder, which should ultimately help both them and the shareholders get a better deal.¹⁶² This, in turn, should allow directors to focus on the

161. See *supra* Part III.B.2.

162. Some notable scholars oppose the view that a pro-target regime and takeover defenses help directors be better negotiators on shareholders' behalf. See Subramanian, *supra* note 60. My claim is that a pro-target regime, absent corporate law collateral factors contributing to director entrenchment, would effectively give directors the advantage of timing and a better mastering of the proxy machinery. I agree these are not enormous advantages, yet they still provide something directors can count on when responding to an unsolicited bidder, especially if compared with the opposite scenario of board passivity where voting inertia favors bidders. Note that the two default regimes are not materially different, but for the corporate law collateral factors. One could object in theory that timing may actually give directors a big advantage in the pro-target regime, as in some circumstances they could dispose of crown jewels of the company quickly in order to dissuade a bidder from pursuing the planned acquisition. See *supra* note 125, for an example of this discussed in the context of the Exact Sciences deal. However, with respect to Delaware, this objection would be valid only for circumstances in which the disposition of crown jewels would neither trigger *Revlon* (and therefore kick the target out of *Unocal* and *Unitrin*, which is what this article focuses on) nor a stockholder vote under Section 271 of the DGCL, which in turn would neutralize the director primacy warranted by *Unocal* and *Unitrin*. See DEL. CODE ANN. TIT. 8, § 271 (2014); *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361 (Del. 1995); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986); *Unocal v. Mesa Petroleum*, 493 A.2d 946 (Del. 1985); see also *supra* notes 94-96 and accompanying text. In other words, the size of the crown jewel must not be too significant. In the case of a divestiture of a core asset of a size *not* sufficient to trigger any such regime or provision, *but* sufficient to dissuade a bidder from continuing with the acquisition plan, we would be dealing with a faux corporate control transaction. What the bidder would really be pursuing in this scenario is a specific asset of the target—directors are generally subject to the business judgment rule as to when and to

business rather than spend too much time worrying about takeovers and pre-planning defenses.¹⁶³

The pro-target default regime leaves shareholders powerless in a series of circumstances.

When a company has an effective staggered board, the likelihood of a reversal of the default by shareholders is very remote—coupled with a staggered board, the pro-target regime ends up promoting managerial entrenchment.¹⁶⁴

When shareholders cannot call special meetings or act by written consent, a target is potentially subject to the risk of a hostile takeover only in certain periods within a year—the risk of entrenchment in this case is arguably less relevant, although it can pose certain risks in control contests that fall outside the *Revlon* zone.¹⁶⁵

Leaving aside staggered boards, which as noted earlier¹⁶⁶ are present in 45.8% of Delaware public corporations (15.5% in terms of market capitalization), data on takeover activity for Delaware companies seem to indicate that a pro-target regime has somewhat worked thus far, in that it has not insulated directors entirely, it has provided a tool to negotiate for higher takeover premiums and still leaves shareholders the opportunity to weigh and act upon the merits of the bid.¹⁶⁷ In light of

whom to sell core assets. *See generally* Hollinger, Inc. v. Hollinger Int'l, Inc., 858 A.2d 342 (Del. Ch. 2004) (illustrating the ability of a board to sell a core asset without the need for shareholder approval under Section 271 of the DGCL). *But see* Katz v. Bregman, 431 A.2d 1274 (Del. Ch. 1981).

163. *See* Coates, *supra* note 26, at 1190 (“[I]f US takeover experience has any lessons, it is that top managers worry about few things more than preserving the control of their firms”); *see also infra* note 172 and accompanying text.

164. As anticipated, a proposed solution for this problem is that if a bidder wins the first election, it should be considered a referendum on the offer, and the board should be forced by the judge to redeem the pill. *See* Bebchuk, Coates & Subramanian, *supra* note 52, at 944-45. While casting several doubts on the policy merits of staggered boards, the Delaware Court of Chancery did not follow such a proposal in *Airgas*. *Air Prods. & Chems., Inc. v. Airgas, Inc.*, 16 A.3d 48, 89 (Del. Ch. 2011). Incidentally, as previously mentioned in the context of the attempted acquisition of *Airgas*, the newly-elected directors, who were all nominated by the bidder, voted unanimously with the rest of the target board to keep the poison pill in place. *See also supra* note 54.

165. *See supra* Part III.B.1.a.

166. *See supra* Part III.C.

167. *See* John C. Coates IV, *Empirical Evidence on Structural Takeover Defense: Where Do We Stand?*, 54 U. MIAMI L. REV. 783, 797 (2000) (analyzing empirical studies published between 1986 and 2000 and finding that “Delaware courts should take some comfort from the fact that they resisted strong academic arguments and

this, the debate on shareholder adopted bylaws to let shareholders have a say on pills prior to a bid being actually on the table,¹⁶⁸ is less relevant, at least for companies without a staggered board, than its proponents would acknowledge.

Another unintentional consequence of a pro-target regime is that if corporate law rules are not flexible enough to permit structural defenses,¹⁶⁹ directors would be empowered to react, but would only have the option to adopt transactional defenses, which might not be an effective response against low ball offers and/or might be detrimental to the company and its shareholders. This problem is of course exacerbated if a jurisdiction lacks adequate fiduciary duties or an effective enforcement system to police directors and management, since in such a case they would have a blank check to engage in wasteful transactions that are aimed only at preserving their power.

B. THE PRO-SHAREHOLDER REGIME IN LIGHT OF THE CORPORATE LAW COLLATERAL FACTORS

The pro-shareholder regime would do a better job at tackling managerial agency costs, since, no matter how easy it is to get shareholders to approve defenses, managers would psychologically perceive the threat of a takeover as more imminent and will work harder to keep stock prices high and make a takeover more difficult.¹⁷⁰ Indeed, under the regime, companies have to go to the trouble of getting shareholders to approve defenses, with all the consequences that this effort may generate (i.e., a potential drop in the stock price). Particularly for jurisdictions where proxy access is suboptimal and/or corporate law is otherwise incapable of policing directors and managers—in jurisdictions where a pro-target approach would create a formidable shield for directors—a pro-shareholder regime would be superior, for purposes of curbing agency costs. However this would come at a price:

political efforts that attempted to push them to dramatically repudiate pills and other structural defenses. The empirical case against defenses . . . is not as compelling as it might have seemed to hostile commentators.”); *see also* Barry & Hatfield, *supra* note 26, at 637, 654 (presenting a model predicting that poison pills increase target shareholder returns).

168. *See supra* Part I.C.

169. Indeed, this clearly is not the case for Delaware—and several other state jurisdictions in the United States, for that matter.

170. This is the main point made by the theorists of board passivity. *See* Easterbrook & Fischel, *Proper Role*, *supra* note 29, at 1174; *see generally supra* note 27.

when corporate law rules are not flexible enough to permit structural defenses, bidders have a clear advantage, since shareholders would sometimes be stuck between two suboptimal choices—whether to accept the bid or approve a value wasting transactional defense. This might result in an excess of acquisition transactions with a low premium, which is an undesirable policy outcome.

Another consequence of the pro-shareholder approach is that, if directors and management perceive they are at risk, given they do not have adequate post-bid responses, they might spend too much time and resources to put pre-takeover defenses in place. By trying to limit their discretion pending a bid, the pro-shareholder approach ends up inducing directors, who have a natural antipathy to any unsolicited acquisition proposal,¹⁷¹ to make the company takeover-proof via other means. For instance, some authors have stressed that directors could abusively agree to change-of-control provisions in the company's core agreements (joint ventures, credit agreements, bond indentures, employment agreements, intellectual property licenses, etc.) to dissuade, or create an additional and significant financial burden on, a potential acquirer.¹⁷²

171. See *Moran v. Household Int'l, Inc.*, 500 A.2d 1345, 1350 (Del. 1985) (describing methods utilized by target companies to forestall undesirable takeover activity); see also Coates, *supra* note 26, at 1190 (“[I]f US takeover experience has any lessons, it is that top managers worry about few things more than loss of control.”).

172. See Jennifer Arlen & Eric Talley, *Unregulable Defenses and the Perils of Shareholder Choice*, 152 U. PA. L. REV. 577, 614 (2003). The problematic aspect of pre-bid defenses is that it is complicated to detect a defensive element in the context of transactions management enters into during peaceful times. Even more complicated is to prove that such defensive element represents the ultimate purpose of the given transaction. As a result, given the unlikelihood a pre-bid defense will end up being judicially second guessed at some later stage (that is, when a bid is on the table), such defenses are riskier in that they can be potentially adopted in an unleashed manner by management, especially if management cannot count on effective defensive tools once a bid is launched. For recent transactions entered into in the context of a larger M&A deal that had the potential of deterring unsolicited bids—however, notably in the context of the legitimacy of a hidden lock-up under *Revlon*—see the \$3.1 billion convertible bond issued by SprintNextel to Softbank in October 2012 (if converted, Softbank would have obtained an approximately 20% stake in the target) and the NYSE/ICE deal for Liffe, NYSE's European derivatives unit, to clear its trades through ICE for at least two years (both transactions would stand irrespective of whether the larger underlying M&A deals closed). See also Jodi Xu & Jeffrey McCracken, *Dish May Face Additional \$1.2 Billion Sprint Cost*, BLOOMBERG (June 14, 2013), <http://www.bloomberg.com/news/2013-06-14/dish-may-face-additional-1-2-billion-sprint-cost.html>; David Benoit, *Security Detail Protects NYSE Deal*, WALL ST. J. (Jan.

Pre-bid defenses are not the sole concern associated with the collateral effects of a pro-shareholder default regime. Such a regime might affect ownership structures, possibly leading to more concentration of stock ownership.¹⁷³ First, incumbents (shareholders having working control of a company or managers themselves) may be tempted to secure a more stable controlling position by building blocks so as to limit or avoid unsolicited bids altogether.¹⁷⁴ Second, the fear of leaving control up for grabs might convince companies to create dual-class voting structures,¹⁷⁵ sell smaller stakes at the IPO stage, or to stay away from capital markets to begin with.

C. SUMMARY AND POLICY REMARKS

The assessment of the two different regimes in relation to various corporate law collateral factors shows that there is no regime on its face that is clearly preferable over the other in awarding shareholders the power (or some power) to determine the outcome of an acquisition. Nonetheless, the analysis demands some policy considerations.

On one hand, factors limiting the reversibility of a regime should be eliminated. This statement is less justified by the fact that reversibility is *per se* good policy than by acknowledging that once a shareholder vote is contemplated as the principle (or, as in Delaware, the last) safeguard, it is not good policy to let collateral aspects jeopardize the process. Therefore, the elimination of obstacles to the free and clear exercise of shareholder vote should be the goal of policymakers whose intention is to give shareholders a critical say on an acquisition outcome. First, a

30, 2013), <http://online.wsj.com/article/SB10001424127887323926104578274112350462452.html>.

173. Enriques & Gatti, *supra* note 86, at 29. *See, e.g.*, Cools, *supra* note 116, at 756-57 (exemplifying a similar approach, albeit in connection with the allocation of corporate powers more generally (and not just in the takeover context)).

174. Enriques & Gatti, *supra* note 86, at 29 n.141 (noting that “[b]uilding blocks can either facilitate the approval of defensive tactics by the shareholders’ meeting or, more simply, make the control of the company not contestable to begin with”).

175. Jeff Green & Ari Levy, *Zuckerberg Grip Becomes New Normal in Silicon Valley*, BLOOMBERG (May 7, 2012), <http://www.bloomberg.com/news/2012-05-07/zuckerberg-stock-grip-becomes-new-normal-in-silicon-valley-tech.html>; *see also* WILMERHALE, 2013 M&A REPORT 14-15 (2013), *available at* www.wilmerhale.com/uploadedFiles/WilmerHale_Shared_Content/Files/Editorial/Publication/2013-wilmerhale-ma-report.pdf (showing the continued trend of new firms going public with several defensive measures, such as staggered boards, multi-class capital structures, and limitations to call special meetings).

simple majority principle should apply to any shareholder vote to decide whether the bid should succeed; otherwise, supermajority provisions give minorities an unwarranted veto power. Second, staggered boards should not alter the outcome of a vote on the bid. As some legal commentators have argued, in the context of a takeover attempt combined with a proxy contest to renew a slot of directors, a shareholder vote to replace incumbents should be considered a referendum in favor of the bid; the remaining directors should not continue to veto the bid. Instead, they should redeem the pill.¹⁷⁶ Third, proxy access and conflict of interest rules should give no clear advantage to any side and should be carefully reconsidered when they apply to the takeover situation.

On the other hand, the types of defenses that may be adopted by companies can impact policy choices. If structural defenses are available, both regimes achieve valuable policy goals (assuming they can be easily reversed).¹⁷⁷ Conversely, if structural defenses are not available, both regimes have significant drawbacks, such as not providing an effective response against low-ball bids, leading to value wasting transactional defenses and, in a pro-shareholder regime, creating incentives to adopt pre-bid defenses.¹⁷⁸ Therefore, the problem of the optimal allocation of corporate powers when deciding on the fate of an unsolicited bid and the problem of the defenses a corporation can adopt should each be considered by a comprehensive policy reform.¹⁷⁹

176. Bebchuk, Coates & Subramanian, *supra* note 52, at 944-45.

177. The pro-target approach facilitates management's bargaining for higher takeover premiums, while the pro-shareholder approach curbs agency costs. Note that the easier it is to reverse a regime with a shareholder vote, the less important the default is and the less effective it is in the attainment of the policy goals the default is meant to pursue.

178. See Arlen & Talley, *supra* note 172, at 603-13.

179. It is very important for shareholders to be able to rely on devices that allow them to vote against an acquisition attempt without having the company entertain disruptive defensive actions. Once shareholders are empowered to approve defensive actions, one should assume that a jurisdiction attaches some positive function to defenses, and thus, there should be no reason for permitting only a limited set of defenses and excluding those that are in the best interests of shareholders. In other words, all else being equal, once a jurisdiction allows takeover defenses, as in the Delaware and United Kingdom systems, giving more options to companies should help them to allow shareholders make the most effective choice on the bid. The possible objection that more discretion might result in more mistakes reflects a paternalistic view of the corporate world, which should not be taken into consideration especially if

I do not intend to endorse the proposition that giving shareholders a critical say in an acquisition (no matter whether the default initially favors them or the directors) is better policy than an alternative system in which shareholders have no say whatsoever (not including Delaware,¹⁸⁰ at least absent staggered boards and other entrenching corporate law collateral factors, but arguably some other state jurisdictions, such as Georgia, Maryland, Pennsylvania and Virginia¹⁸¹). That conclusion is not central to my thesis here, which is to raise awareness of the impact of corporate law collateral factors.

Some scholars have recently argued that policymakers should leave it to companies to decide the “who decides” question as to whether a takeover should go through or not.¹⁸² In the past, in the context of analyzing the Takeover Bids Directive, I have shown sympathy for a

one assumes directors have fiduciary duties and other ex-post sanctions (and a good enforcement system) in place.

180. Interestingly, although Delaware allows board insulation and entrenchment via corporate law collateral factors such as staggered boards, it does not allow corporations to opt out of *Unocal* and *Unitrin* altogether (not even, it would appear, on a temporary basis with sunset arrangements) as that would violate the *Quickturn* doctrine. *Quickturn Design Sys. v. Shapiro*, 721 A.2d 1281, 1293 (Del. 1998); *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361 (Del. 1995); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985); see *supra* note 78 and accompanying text. The DGCL does not grant corporations the contractual freedom to select entrenchment openly, yet it does not interfere with directors’ de facto ability to insulate themselves through other means (the corporate law collateral factors).

181. See Subramanian, *supra* note 60, at 628 (noting how these states have validated either dead hand or slow hand pills, which “are far more potent than the plain vanilla pills that are valid in Delaware; the dead hand pill in particular [which is valid in Georgia, Pennsylvania, and Virginia,] is generally understood to be a complete defense against a hostile takeover bid”).

182. Enriques, Gilson & Paces, *supra* note 92, at 12-14. In support of this view is the line of thought that the diverse defense levels that corporations show can be explained because: (i) corporations with the highest expected synergies should be the most likely to have effective staggered boards—that would include highly technology-intensive companies and companies with nontraditional businesses; (ii) defenses appear more frequently among firms in industries where takeovers are more common and in which managerial performance is easier to observe; and (iii) staggered boards increase value when firms have higher advisory needs (that is, large and complex firms) and low monitoring costs. See Barry & Hatfield, *supra* note 26, at 654, 693-95 (citing various empirical studies, including Robert Daines & Michael Klausner, *Do IPO Charters Maximize Firm Value? Antitakeover Protection in IPOs*, 17 J.L. ECON. & ORG. 83, 96 tbl.2 (2001)).

somewhat similar approach.¹⁸³ However, the importance for policymakers to acknowledge and address the corporate law collateral factors cannot be stressed enough. If all companies are deciding on in fact the “who decides” question, while neglecting such other factors (some of which they admittedly control, such as factors that can be determined at the charter or bylaws level, some others they do not, such as certain mandatory rules that are generally set by the legislators—e.g., the regime on shareholders’ conflict of interest or the proxy rules), the benefits of letting companies determine what takeover rules they should be subject to would be partial at best, if not minimal. In other words, there can be no effective takeover reform without expressly addressing all the potential issues raised by the corporate law collateral factors.¹⁸⁴ Needless to say, interpreters of applicable positive law should also address the impact of corporate law collateral factors and possibly distinguish cases and tweak existing standards based on that.

A final note: in Delaware companies are *already free* to decide the level of corporate law collateral factors they intend to be subject to, yet in practice this means that choices can for the most part be expressed only at the IPO-stage by founders/managers: as soon as the company goes public the rules governing charter amendments are such that they create a perennial impasse given the reciprocal veto power of directors and shareholders (each category having to approve the amendment

183. See Gatti, *supra* note 6, at 568-69 (arguing an optional system is better than a mandatory system in the EU); *id.* at 570-71 (arguing that “a pro-takeover default is preferable, as it requires targets to take steps to reverse it, which is something that may have a negative impact on stock prices and will shine a spotlight on targets that try to hide, whereas, in the case of the adoption of a pro-[target] default, the market will quite certainly not expect that many ‘virtuous’ targets will take actions to reverse it”). I note incidentally that even though the optional pro-takeover default I advocated was not expressly contemplated by the Takeover Bids Directive, I nonetheless concluded that Member States could actually adopt it on their own, as in my view such solution would not materially depart from the Directive. *Id.* at 571. Note that, starting in 2009, Italy has in fact adopted such a solution: the board neutrality rule is a default rule companies can opt out of if they so choose. See, e.g., Enriques, Gilson & Paces, *supra* note 92, at 40 n.131 (noting that FIAT, a leading Italian automaker, opted out of the board neutrality rule).

184. See Luca Enriques, *European Takeover Law: The Case for a Neutral Approach*, 22 EUR. BUS. L. REV. 623, 638-39 (2011) (discussing the topic from an EU reform standpoint and conceding that “we cannot expect the EU to revise all company and securities law rules having an even more indirect effect on takeovers”).

pursuant to Section 242(b)(1)-(2) of the DGCL).¹⁸⁵ The results are quite absurd: each Delaware company is subject to a static regime it chose once and for all at the IPO-stage, with very little chance to further adapt to changes (market changes, preference changes, etc.). Policy proposals seeking to affect the power to decide on takeovers must not only consider the corporate law collateral factors I identify, but must also consider the process by which these factors are selected. The proper perspective is a dynamic one: one that takes into account not only rules governing the initial selection of the takeover regime *cum* collateral factors, but also (new) rules governing the power to alter this initial selection. Mandatory re-openings and sunsets are the first solutions that come to mind, yet the optimal way to address Section 242-type reciprocal vetoes is something that begs for in-depth study.

CONCLUSION

Without “corporate law collateral factors,” such as shareholders’ ability to call special meetings or act by written consent, the presence of supermajority provisions, biased proxy rules, ineffective rules policing shareholders’ conflict of interest, staggered boards and director removability, the two seemingly opposite anti-takeover regimes in Delaware and in the United Kingdom would lead to the same acquisition outcomes. Therefore, most of the debate on the best takeover policy would miss the point that the regimes in themselves are rather immaterial but for those factors, which make the real difference between the two approaches.

Ultimately, there has been too much emphasis on the allocation of the power to decide on acquisitions and too little on other external rules, the corporate law collateral factors, which have bigger effects on the intended policy purpose that under each regime purports to give shareholders the decisive (or at least some critical) power to determine the outcome of the acquisition. With the notable exception of staggered boards, not enough attention has been given to the barriers to reversibility of the takeover default regime that such collateral factors raise.

If a jurisdiction is serious about fostering shareholder powers in the context of an acquisition, rather than just determining which way to set the default, policymakers should focus on eliminating, or containing the

185. See DEL. CODE ANN. TIT. 8, § 242(b)(1)-(2) (2014) (requiring all changes to certificate of incorporation be approved by both the board and the shareholders).

reach of, such barriers. Also, if a jurisdiction is serious about takeover regulation in general, policymakers should consider addressing all corporate law collateral factors within the body of takeover law (whether or not statutory). Given the importance of takeovers, it is odd not to discuss tailored rules (applicable in the takeover context only and explicitly preempting basic corporate law principles) for such subjects as shareholders' conflicts of interest, proxy rules, availability of poison pills, and so forth. Leaving the corporate law collateral factors to general corporate law does a disservice to takeover players and stakeholders.