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State Regulation of Tender Offers: Legislating Within the Constitutional Framework

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STATE REGULATION OF TENDER OFFERS: LEGISLATING WITHIN THE CONSTITUTIONAL FRAMEWORK

INTRODUCTION

In Edgar v. MITE Corp., the Supreme Court held that the Illinois Business Takeover Act imposed a burden on interstate commerce that outweighed any local interest served by the law. In accord with this case, courts struck down many local tender offer statutes. One state refused to renew its law. Thus, MITE Corp. has cast doubt on the states' ability to regulate tender offers effectively.

3. MITE Corp., 457 U.S. at 646 (White, J.). The Chief Justice joined Justice White. Justices Powell, Stevens and O'Connor filed separate opinions, concurring with this part of Justice White's commerce clause analysis. Id. at 646-55. Justice White thought that the most obvious burden the Illinois Act imposed on interstate commerce was that it purported to give the state the ability to prohibit a tender offer anywhere in the country. See id. at 643. The majority's opinion chilled any hopes states may have had of protecting corporations from nationwide takeovers. The Court made it clear that states have no legitimate interest in regulating out-of-state transactions. Id. at 644. State tender offer legislation must be for the sole protection of local investors. Compare id. (Illinois statute purported to suspend takeovers on a nationwide basis) with Cardiff Acquisitions, Inc. v. Hatch, 751 F.2d 906, 911 (8th Cir. 1984) (under Minnesota statute any suspension of the tender offer applies only to state residents).
6. The Court's use of the Pike balancing test, see MITE Corp., 457 U.S. at 643, implies that there is some room for states to regulate tender offers, see id. at 646 (Powell, J., concurring), but just how much room there is remains uncertain. The majority held that the Illinois statute did not produce sufficient benefits to outweigh the burden it placed on interstate commerce. See id. at 644-45 (disclosure required by the Illinois Act did not put resident shareholders in a better position to make an informed decision when faced with a tender offer). Because many takeover disclosure acts were similar, see Newlin & Gilmer, The Pennsylvania Shareholder Protection Act: A New Approach to Deflecting Corporate Takeover Bids, 40 Bus. Law. 111, 111 (1984), the Illinois Act was not alone in its constitutional encroachments, see National City Lines, Inc. v. LLC Corp., 687 F.2d 1122, 1128 (8th Cir. 1982) ("[o]ur examination reveals that there are no significant distinctions between the Illinois and Missouri Takeover Acts"). Justice White, with Chief Justice Burger and Justice Blackmun, held that because Congress chose to remain neutral in takeover battles, states could not pass laws that favored management over the offeror. See MITE Corp., 457 U.S. at 631-40 (1982). Two Justices disagreed with this rationale,
Some local legislatures responded by attempting to bring existing statutes within constitutional guidelines. Others drafted new laws shifting the regulatory focus from the purchase of securities to the "business combinations" that often follow a successful takeover.

This new legislation raises questions. States must apply the statutes constitutionally. Moreover, laws affecting business combinations may violate the supremacy clause because they discourage tender offers.

This Note will examine the constitutional limitations on state takeover statutes. Part I discusses the Williams Act and state takeover statutes. Part II sets out the constitutional analysis courts use to scrutinize state tender offer legislation. Part III examines the clashes between takeover legislation, past and present, and the Constitution. Part IV traces the limits on the states' ability to regulate tender offers.

This Note concludes that states may regulate takeover bids, but only to protect local investors. Local legislators cannot protect corporations from hostile tender offers. The commerce clause permits states to regu-


10. See infra notes 85, 133, 134, 152 and accompanying text for state statute provisions that present problems.

11. "Because we find that the Act is ... constitutional on its face, we must also analyze whether the Act is constitutional as applied by the Commissioner." Cardiff Acquisitions, Inc. v. Hatch, 751 F.2d 906, 914 (8th Cir. 1984).

12. See infra note 133.

late only offers for "state corporations" to local residents. In addition, to avoid conflicts with the supremacy clause, state legislation must conform with the letter and spirit of the Williams Act.

I. THE LEGISLATION

A. State Statutes

States use two general classes of statutes to regulate takeovers. First generation statutes regulate the actual purchase of securities. These laws resemble the Williams Act in both form and substance. However, many of the state acts are better suited to protect incumbent management than local investors, while the purpose of the Williams Act is to protect shareholders.


15. Sargent, supra note 14, at 3-4.

16. Id. A comparison between the first Ohio Takeover Act, Ohio Rev. Code Ann. §§ 1707.04.1-.04.2 (Page 1985), and the Williams Act, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1982), shows that the laws were analogous. The statutes require almost identical disclosures in some instances.

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<th>Ohio Act</th>
<th>Williams Act</th>
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<td>1) Source and amount of the funds or other consideration used or to be used in making the purchases.</td>
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<td>3) Background, identity, residence, citizenship, nature nature of beneficial ownership of persons on whose behalf transactions are to be effected.</td>
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17. See Sell, supra note 6, at 475.

18. See infra notes 26, 33, 118, 120, 121 and accompanying text.
Second generation statutes do not directly regulate the purchase of securities. These statutes are part of state general corporation law and usually regulate business combinations. For example, the Maryland law requires a successful offeror intending a "business combination" either to obtain the approval of a supermajority of the disinterested shareholders or to pay a "fair price" to nontendering shareholders forced to sell in the course of the business combination. This statute inhibits front-end-loaded two step takeovers on the theory that such bids are inherently unfair to nontendering shareholders. Section 912 of the New York Business Corporation Law also restricts post-tender offer "business combinations."

B. The Williams Act

Congress adopted the Williams Act in 1968 in response to the growing use of tender offers as a means of capturing control of a corporation. The Act protects investors by requiring persons seeking control of a corporation through tender offer, open market or privately negotiated purchases of securities, to disclose relevant information to the target's stockholders. This information includes the source of the funds the offeror is using for the purchases, the purposes of the purchases, and the background, identity, residence and citizenship of any person on whose behalf the offeror makes purchases.

In addition to disclosure requirements, the Act contains provisions designed to mitigate the coercive influences of a tender offer. For example, the seven-day withdrawal and pro rata pick-up provisions re-

22. The two tier offer is really a single offer to acquire full control of a corporation. The first step typically involves a cash offer for some of the target's shares. In the second step, the offeror acquires the rest of the target's shares for securities worth less than the cash paid for the first block of shares. Thus, the offer is front-end loaded. See Note, Front-End Loaded Tender Offers: The Application of Federal And State Law To An Innovative Corporate Acquisition Technique, 131 U. Pa. L. Rev. 389, 389 (1982).
28. See id. § 78m(d)(5)-(8).
29. See id. § 78n(d)(5) (a person who deposits shares pursuant to a tender offer can
move some of the incentive to sell in haste allowing investors to consider more carefully the decision to tender their shares.\textsuperscript{31}

The Act favors neither incumbent management nor the offeror;\textsuperscript{32} it promotes a federal policy of neutrality in takeover contests. Congress did not intend the Williams Act to be a weapon that targets could use to defeat tender offers.\textsuperscript{33} The lawmakers did not wish to discourage tender offers.\textsuperscript{34} On the contrary, the lawmakers viewed takeovers as a check on entrenched but inefficient management.\textsuperscript{35} The Williams Act's function is to get information to investors by allowing both sides to present their arguments.\textsuperscript{36} The Williams Act preempts any state statute that frustrates the full accomplishment of its policies or purposes.\textsuperscript{37}

II. CONSTITUTIONAL FRAMEWORK

Many state statutes are invalid either in whole or in part because they violate the commerce or supremacy clauses.

withdraw those shares at any time up to seven business days after definitive copies of the tender offer are published or given to security holders).

30. See id. § 78n(d)(6) (When the offer is for less than all the outstanding equity shares of a class and more are tendered than the offeror is willing to take, the offeror will take shares deposited within ten days of the offer's publication on a pro rata basis. This removes some pressure on shareholders to tender immediately for fear of being frozen out of the offer.).

31. The Securities and Exchange Commission extended the seven day period to 15 days pursuant to its rule-making authority under the Act. See 17 C.F.R. § 240.14d-7(a)(1) (1985). The extension gives the security holders more time to consider the decision to deposit their shares. See 44 Fed. Reg. 70,334 (1979).

The pro rata pick-up requirement is designed to outlaw the first-come, first-served tender offer and eliminate pressure on shareholders to deposit their shares hastily. 113 Cong. Rec. 856 (1967) (remarks of Sen. Williams).

32. See infra note 120 and accompanying text.

33. Rondeau v. Mosinee Paper Corp., 422 U.S. 49, 58 (1975); see 113 Cong. Rec. 24,664 (1967) (remarks of Sen. Williams) ("We have taken extreme care to avoid tipping the scales either in favor of management or in favor of the person making the takeover bids."); id. at 854 (remarks of Sen. Williams) ("Every effort has been made to avoid tipping the balance of regulatory burden in favor of management or in favor of the offeror.").


A. Preemption

The supremacy clause makes federal law paramount. State legislation interfering with or contrary to the laws of Congress is invalid.

Though simply stated, preemption analysis involves more than applying doctrine to facts. The courts often have to balance state and federal interests in regulating a particular activity. Courts can invalidate state laws under any one of three theories, but warn that "there can be no one crystal clear distinctly marked formula.

Courts can find that federal law preempts state law if Congress expressly manifests its intent that the federal law do so. The lawmakers did not expressly prohibit states from regulating tender offers. On the contrary, section 28(a) of the Securities Exchange Act of 1934—to which the Williams Act is an amendment—provides in pertinent part:

Nothing in this title shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this title or the rules and regulations thereunder.

Because Congress allowed the states to regulate tender offers, state takeover statutes will violate the supremacy clause only if they conflict with the Williams Act.

38. U.S. Const. art. VI, cl. 2.
Under a second theory, a court may infer congressional intent to preempt state law. The courts will draw this inference when the interests involved are so intrinsically federal that it is reasonable to assume that states may not regulate the subject, or the federal legislation is so pervasive as to indicate there is no room for supplemental local regulation. Because Congress expressly gave states permission to regulate tender offers, courts will not infer congressional intent to preempt local statutes.

Finally, a court will also invalidate a state law if it conflicts with a congressional mandate. A conflict arises when compliance with both state and federal law is impossible or when the local legislation stands as an obstacle to the accomplishment of congressional purposes. Courts have used the "obstacle" theory to scrutinize state takeover legislation. When a state statute frustrates the full accomplishment of Congress' objectives in adopting the Williams Act, it is preempted.

Justice White, expressing the views of a plurality of the Court in *MITE Corp.*, stated that the Illinois Business Takeover Act was preempted because it stood as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress. Though only two Justices...
concurred in this part of Justice White's opinion, the analysis was not rejected by a majority and has been used by lower courts when examining state tender offer legislation.

This last supremacy clause analysis is useful in looking at first and second generation statutes because both are capable of frustrating the Williams Act's policies. This kind of scrutiny will be applicable to second generation legislation because, while states have avoided textual conflicts between their statutes and the Williams Act, some cling to pro-management policies.

In MITE Corp., the Court did not consider the extent to which compliance with both the Illinois statute and the Williams Act was impossible. However, this inquiry is part of supremacy clause jurisprudence and lower courts have used it when examining state takeover legislation.

Even if a state takeover statute comports with the supremacy clause, it may still impermissibly burden interstate commerce, and therefore be invalid.

B. The Commerce Clause

The commerce clause gives Congress the power to "regulate Commerce . . . among the several states." This grant of authority to the federal government also imposes a restraint on state legislatures. States

60. See id.
61. Justice Powell and Justice Stevens disagreed with Justice White's supremacy clause analysis. They did not believe that Congress' choice to remain neutral in takeover contests obliged the states to adopt the same policy. See id. at 646-47 (Powell, J., concurring). Justices Brennan, Marshall, O'Connor and Rehnquist failed to reach the issue. See supra note 6. See Cardiff Acquisitions, Inc. v. Hatch, 751 F.2d 906, 909 n.1 (8th Cir. 1984).
63. New York recently enacted legislation designed to promote the long-term growth of local corporations. One of the effects of the law will be to discourage unilateral takeovers that depend on the target's assets to finance the deal. Governor's Program Bill Memorandum for 1985 Extraordinary Session at 1, 8; see N.Y. Legal Times, Jan. 20, 1986, at A1, col. 4, A15, col. 4.
66. U.S. Const. art. I, § 8, cl. 3.
67. Id.
68. Lewis v. BT Inv. Managers, Inc., 447 U.S. 27, 35 (1980); Great Atl. & Pac. Ten Co. v. Cottrell, 424 U.S. 366, 370-71 (1976); see also Freeman v. Hewit, 329 U.S. 249, 252 (1946) ("[T]he Commerce Clause was not merely an authorization to Congress to enact laws for the protection and encouragement of commerce among the States, but by its own force created an area of trade free from interference by the States.").
may not directly regulate or restrain interstate commerce. Moreover, a local government cannot interfere with commerce that takes place wholly outside its borders.

However, not all state regulation of interstate commerce is invalid. When a statute regulates evenhandedly to further a legitimate public interest and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on commerce is clearly excessive in relation to the putative local benefits.

Citing a legitimate interest is not enough. State legislators must draft statutes that produce local benefits without needlessly burdening commerce. Many early attempts at local tender offer legislation failed on this point.

The MITE Court found that the Illinois Business Takeover Act imposed excessive burdens on interstate commerce relative to the benefits to the state. Justice White, writing for the Court, used the balancing test of *Pike v. Bruce Church, Inc.* to reach his conclusion. Under the test, courts balance the burden a statute places on interstate commerce against the benefits to the regulating state. The extent of the burden the courts will tolerate depends on the nature of the local interest involved and whether it can be achieved with less impact on interstate activities.

Many first generation statutes allowed state officials to suspend tender offers on a national level if the bidder did not comply with state law.

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69. See Arkansas Elec. Coop. v. Arkansas Pub. Serv. Comm'n, 461 U.S. 375, 378 (1983) ("We struck down the regulation . . . because it . . . imposed a 'direct' rather than an 'indirect' burden on interstate commerce."); The Minnesota Rate Cases, 230 U.S. 352, 396 (1913) ("If a state enactment imposes a direct burden upon interstate commerce, it must fall.") (emphasis in original); Brennan v. Titusville, 153 U.S. 289, 302 (1894) ("[N]othing which is a direct burden upon interstate commerce can be imposed by the State."). Four Justices in *MITE Corp.* agreed that the Illinois Business Takeover Act directly regulated commerce because it applied to transactions taking place across state lines. The statute even applied to transactions effected totally outside the state's borders. In fact, the Act could have applied to a tender offer that did not involve a single Illinois resident. See Edgar v. MITE Corp., 457 U.S. 624, 640-43 (1982) (plurality opinion of White, J.).


75. *MITE Corp.*, 457 U.S. at 643.


77. *Pike*, 397 U.S. at 142.

78. See, e.g., Pub. Act No. 80-556, § 11(H) (to be codified at Ill. Ann. Stat. ch. 121½,
These statutes failed under the *Pike* test because the extent of the burden on commerce was great, and the state could have protected local investors without suspending the tender offer outside its borders.\textsuperscript{79}

Justice White also thought the Illinois act violated the commerce clause by directly regulating interstate commerce.\textsuperscript{80} And although the majority did not go along with that part of his opinion,\textsuperscript{81} a district court in *Icahn v. Blunt*\textsuperscript{82} used this theory to strike down a Missouri takeover statute.\textsuperscript{83}

Second generation statutes regulate commerce indirectly\textsuperscript{84} and so should be analyzed under the *Pike* test. The result of the analysis is uncertain because the courts have yet to determine the burden imposed by these statutes. It is clear, however, that second generation statutes make some kinds of takeovers more difficult. For instance, if the bidder needs the captured corporation's assets to finance the tender offer, restrictive merger provisions effectively prevent the takeover.\textsuperscript{85} Whether the local benefits of these statutes will tilt the scale in the states' favor remains to be seen.\textsuperscript{86}

\textsuperscript{79} See *MITE Corp.*, 457 U.S. at 644. The majority in *MITE Corp.* noted that states have no legitimate interest in protecting out-of-state shareholders. Therefore, the state gets no benefit from protecting nonresident investors and there is nothing to weigh against the statute's harmful effects on interstate commerce. *Id.*

\textsuperscript{80} See *id.* at 640-42 (plurality opinion of White, J.).

\textsuperscript{81} The Chief Justice joined Justice White's entire opinion. Justices Stevens and Powell filed separate opinions concurring with this part of Justice White's opinion. See *id.* at 626, 646-47.

\textsuperscript{82} 612 F. Supp. 1400 (W.D. Mo. 1985).

\textsuperscript{83} See *id.* at 1414-17 (Missouri statute prohibiting sales of a control block of shares without approval of a supermajority of the stockholders was a direct regulation of interstate commerce because the law was applicable to foreign corporations and state officials could use it to inhibit transactions between nonresidents).

\textsuperscript{84} See supra note 19.

\textsuperscript{85} See Sargent, supra note 14, at 10 (Maryland statute is designed to inhibit front-end loaded two-tier takeovers); Pinto, *Constitutionality of N.Y.'s New Takeover Statute*, Nat'l L.J., Feb. 24, 1986, at 17, col. 4, at 30, col. 1 (§ 912 of the New York Business Corporation Law may, through its restrictive business combination provisions, prevent takeovers because the offeror would not be able to use the target's assets to leverage the transaction).

\textsuperscript{86} Because the nature of the burdens second generation statutes place on interstate commerce is uncertain, it is impossible to say whether the putative local benefits will outweigh the burdens. In addition, how well second generation statutes promote the states' interests is an important question. If the statutes fail to provide benefits, the burdens they impose on interstate commerce will be hard to justify. For a more detailed discussion, see Sargent, *supra* note 14, at 26-34.
III. CONSTITUTIONAL ANALYSIS OF CURRENT STATE STATUTES

State takeover statutes are of two general types. First generation statutes resembled the Williams Act. They directly regulated the purchase and sale of securities. Courts held many first generation laws unconstitutional after MITE Corp. The statutes' extra-territorial effect violated the commerce clause, and some were counter to the purposes and objectives of Congress. For example, in National City Lines, Inc. v. LLC Corp., the Eighth Circuit held that the Missouri Takeover Bid Disclosure Act was contrary to the commerce and supremacy clauses.

The statute's commerce clause problem was fundamental. The Missouri legislature purported to give the state attorney general the authority to regulate or prohibit a tender offer wherever it might take place. The Act's jurisdictional requirements did not limit its application to Missouri residents. This is a flaw the statute shared with the Illinois law struck down in MITE Corp. Missouri tried to prohibit tender offers to out-of-state investors but, because a state has no legitimate interest in protecting nonresident investors, there was no local benefit to balance against the burden on interstate commerce. Thus, the law excessively burdened interstate commerce.

The Missouri legislation did not fare well under a preemption analysis either. Compliance with the statute and the Williams Act was impossible, because the state and federal timetables did not match. The Mis-

87. See supra note 14.
88. See supra note 4.
89. See supra note 4.
90. 687 F.2d 1122 (8th Cir. 1982).
92. See National City Lines, Inc., 687 F.2d at 1128-33.
93. See Mo. Ann. Stat. §§ 409.505(4)-(5), 409.535 (Vernon 1979). The Missouri legislature defined offeree as a person, whether a shareholder of record or a beneficial owner, to whom a takeover bid is made. See id. § 409.505(4). The statute did not require the offeree shareholder to be a Missouri citizen and thus could reach transactions between shareholders anywhere in the country. The statute also defined offeree company broadly enough to include out-of-state corporations. Therefore, the law covered corporations only loosely tied to the state. See id. § 409.505(5).
94. The statute applied to an offer for shares of a company incorporated in the state or with a principal place of business or executive office there. Id. § 409.505.5(a), (b). Under these standards, a state could exercise jurisdiction over tender offers for companies that have only an office or retail outlet in the state, but not a single local shareholder.
95. National City Lines, 687 F.2d at 1128, 1133. The court stated that because the two statutes were for all practical purposes identical, the Supreme Court's holding in MITE Corp. governed the commerce clause issues presented by the Missouri act. Id. at 1128.
97. Id.
98. Id. at 646.
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souri statute gave management weapons\textsuperscript{100} that tipped the balance of power in contests for corporate control.\textsuperscript{101} This result was contrary to the purposes and objectives of the Williams Act. Therefore, the law violated the supremacy clause.\textsuperscript{102}

Many first generation statutes resembled the Missouri act.\textsuperscript{103} It was clear that states had to find an alternative way to regulate tender offers.

Second generation statutes shift the regulatory focus away from the purchase of securities. They regulate the tender offer through substantive provisions in the general corporation law, specifically those dealing with business combinations.\textsuperscript{104}

Section 912 of the New York Business Corporation Law is an example.\textsuperscript{105} The statute prevents an offeror who gains twenty percent or more of a “resident domestic corporation’s” stock from engaging in certain “business combinations” for five years from the date the bidder gained twenty percent of the stock.\textsuperscript{106} To avoid this prohibition the offeror must gain the approval of the board of directors, prior to becoming the beneficial owner of twenty percent of the shares, for the acquisition of the twenty percent or for any prospective business combination.\textsuperscript{107}

After the five-year period, a New York resident corporation still cannot enter into a business combination with an interested shareholder unless a majority of the disinterested shares approve the deal.\textsuperscript{108} The interested shareholder can escape this proscription if he pays a “fair price” to the minority shareholders.\textsuperscript{109}

Second generation statutes are primarily matters of state corporation law and regulate interstate commerce indirectly. Therefore, the local benefit of one of these laws must outweigh the burden it places on interstate commerce. The extent of the burden a court will tolerate, however,

\begin{footnotes}
\footnotetext[100]{The hearing provision allowed the target to delay the offer. Mo. Ann. Stat. § 409.515.1(2) (Vernon 1979). Delay is a potent weapon in a takeover battle. See infra note 122.}
\footnotetext[101]{National City Lines, Inc., 687 F.2d at 1132-33.}
\footnotetext[102]{Id. at 1128-33.}
\footnotetext[103]{See Newlin & Gilmer, The Pennsylvania Shareholder Protection Act: A New State Approach to Deflecting Corporate Takeover Bids, 40 Bus. Law. 111, 111 (1984). The typical first generation state takeover statute had three main provisions: a precommencement statement of intention provision, an administrative hearing provision and a provision that allowed a state official to suspend the offer if he found it to be unfair. Courts found these provisions contrary to either the supremacy or commerce clauses. Id.}
\footnotetext[104]{See supra notes 19-24 and accompanying text.}
\footnotetext[106]{Id. § 912(a), (b).}
\footnotetext[107]{Id. § 912(b).}
\footnotetext[108]{Id. § 912(c)(2).}
\footnotetext[109]{Id. § 912(c)(3).}
\end{footnotes}
depends on whether the state could attain the same benefit with a lesser impact on interstate commerce.\textsuperscript{110} Many second generation statutes violate the commerce clause because there are less restrictive methods that states could use to achieve their goals.\textsuperscript{111}

The supremacy clause analysis will inevitably depend on whether state and federal policies can coexist. Local statutes that frustrate the policies of the Williams Act are invalid.\textsuperscript{112}

IV. STATE STATUTES THAT WILL SURVIVE CONSTITUTIONAL SCRUTINY

A. Avoiding Preemption

There is room for states to regulate tender offers. However, state statutes must be free of all substantive conflicts with the Williams Act. Provisions that call for prior notification by the offeror to the target company or frustrate any of the federal timetables invite preemption.\textsuperscript{113} Requiring the bidder to warn incumbent management of the impending takeover conflicts with the federal statute. Under the Williams Act, a bidder must commence an offer within five days of making it public.\textsuperscript{114} Laws that require an offeror to warn the target twenty days in advance\textsuperscript{115} make compliance with federal law impossible\textsuperscript{116} because the offeror cannot begin the offer within the five-day period. Precommencement provisions also give management a potent weapon in a takeover battle.\textsuperscript{117}

States must also avoid clashes with congressional policy on takeover bids. The underlying purpose of the Williams Act is to protect investors,
not incumbent management.\textsuperscript{118} Protecting management, or making takeovers more difficult, hurts investors by depriving them of the opportunity to tender their shares at a premium above the market price.\textsuperscript{119} Courts should invalidate state statutes that frustrate the accomplishment of the lawmakers' goals.

It is also clear that Congress was careful to avoid favoring either incumbent management or the takeover bidder.\textsuperscript{120} Thus, states cannot enact laws that undermine this policy of neutrality.\textsuperscript{121} For example, laws that protect management from hostile takeovers by causing delay in the tender offer would conflict with Congress' intent.\textsuperscript{122}

The Williams Act requires extensive disclosure of the facts surrounding a tender offer.\textsuperscript{123} Local legislators can call for disclosure in addition to any prescribed by Congress.\textsuperscript{124} States must, however, be careful not to confuse investors.\textsuperscript{125} The additional facts must be within the spirit of the Williams Act. A state can only require information that will help resident investors make decisions.\textsuperscript{126} State laws cannot require disclosures


\textsuperscript{119} See MITE Corp., 457 U.S. at 633 n.9 ("Congress . . . did not want to deny shareholders 'the opportunities which result from the competitive bidding for a block of stock of a given company,' namely, the opportunity to sell shares at a premium over their market price."). (quoting 113 Cong. Rec. 24,666 (1967) (remarks of Sen. Javits)).


\textsuperscript{121} See supra note 6.


\textsuperscript{123} See 15 U.S.C. § 78m(d)(1) (1982). "All shareholders should have such information so that they can make informed investment decisions on the basis of the same facts known by the person making the tender." 113 Cong. Rec. 855 (1967) (remarks of Sen. Williams); see Edgar v. MITE Corp., 457 U.S. 624, 627-28 n.2 (1982) (The Williams Act "requires disclosure of the source of funds used to purchase the target shares, past transactions with the target company, the other material financial information about the offeror." The bidder must also disclose any legal problems that may result if the takeover is successful.).


\textsuperscript{125} The Williams Act requires extensive disclosure of the facts surrounding a takeover. See supra note 123. Congress, however, was careful to avoid swamping investors with so much information that relevant data would be lost among irrelevant data. See Great W. United Corp. v. Kidwell, 577 F.2d 1256, 1280-81 (5th Cir. 1978) (SEC tries to avoid requiring disclosure of documents that are so detailed that shareholders will not read them), rev'd on other grounds sub nom. Leroy v. Great W. United Corp., 443 U.S. 173 (1979); E. Aranow, H. Einhorn & G. Berlstein, Developments In Tender Offers For Corporate Control 219-20 (1977) (relevant information can be obscured by insignificant disclosures).

\textsuperscript{126} In MITE Corp., Justice White was not convinced that the disclosure the Illinois Act required enhanced a shareholder's position when faced with a tender offer. See Ed-
that would overwhelm the shareholder with a mass of irrelevant information or be excessively burdensome to the offeror.\(^\text{127}\)

In fact, the only significant disclosure local legislators can require is information concerning the effects of the takeover on their state or its residents.\(^\text{128}\) This type of information can help the investor to make an educated choice.\(^\text{129}\)

State tender offer legislation must help the investor to decide whether to tender his shares. This follows federal policy.\(^\text{130}\) Local authorities may not judge the fairness of the offer. That is for the shareholder to decide.\(^\text{131}\) Local officials can require factual disclosure and halt the bid—to state residents only—if they find the facts disclosed are insufficient to

\(^\text{127}\) gar v. MITT Corp., 457 U.S. 624, 644 (1982). Much of the protection the Illinois Act provided was already afforded by the Williams Act. \textit{Id.} at 644-45. \textit{Compare} Cardiff Acquisitions, Inc. v. Hatch, 751 F.2d 906, 913-14 (8th Cir. 1984) (the Minnesota statute generally conforms with the spirit of the Williams Act) \textit{with} National City Lines, Inc. v. LLC Corp., 687 F.2d 1122, 1131-32 (8th Cir. 1982) (the Missouri law conflicted with both the letter and spirit of the Williams Act). The disclosure requirements at issue in \textit{National City Lines} were broad and open-ended. For example, one provision allowed the Commissioner to require any disclosure necessary for the public interest. See Mo. Rev. Stat. § 409.515.2 (1979). Most of the disclosures at issue in \textit{Cardiff} were consistent with the Williams Act. \textit{See} \textit{Cardiff Acquisitions, Inc.}, 751 F.2d at 913-14.

\(^\text{128}\) In \textit{Cardiff}, the Eighth Circuit held that the additional disclosures Minnesota required, with two exceptions, were consistent with the Williams Act. \textit{Cardiff Acquisitions, Inc. v. Hatch}, 751 F.2d 906, 914 (8th Cir. 1984). These additional disclosures concerned the effects of the takeover on the target company’s operations, its employees, suppliers and customers and the communities in which it operates. \textit{Id.}; see Minn. Stat. Ann. § 80B.03(6)(c) (West Supp. 1986). These disclosures are within the purpose of the Williams Act. Congress wanted investors to know what the effects of a takeover would be so that the shareholders could weigh them in making their decisions. \textit{See} \textit{supra} note 123. States can require disclosure that conforms with the spirit of the Williams Act, and helps investors make informed decisions. \textit{Cardiff Acquisitions, Inc. v. Hatch}, 751 F.2d 906, 914 (8th Cir. 1984).

\(^\text{129}\) \textit{See} \textit{supra} note 128.


allow the investor to make an informed choice.132

States cannot enact laws that discourage tender offers. Congress has decided that tender offers check entrenched but inefficient management.133 Many second generation statutes make some types of takeovers impossible134 and are therefore vulnerable to preemption. New state statutes must protect local investors without hampering the tender offer. A statute similar to the Williams Act requiring additional disclosures relevant to local shareholders would protect investors without offending federal policy.

B. Comporting With The Commerce Clause

Local tender offer legislation must not directly affect shareholders outside the state's jurisdiction. Courts can strike down laws with an extra-territorial effect on either of two grounds. They can invalidate the legislation as a direct regulation of interstate commerce135 or find that any indirect burden the statute places on interstate commerce is not outweighed by its benefit to the state.136 Regulations that affect only state residents can promote local interests with a minimal effect on interstate

132. See Cardiff Acquisitions, Inc. v. Hatch, 751 F.2d 906, 914-15 (8th Cir. 1984) (Minnesota Commissioner could not judge the offer's fairness, but could require disclosure to be comprehensive enough to allow shareholders to determine for themselves whether they should retain or sell their stock).

133. See H.R. Rep. No. 1711, 90th Cong., 2d Sess. 4, reprinted in 1968 U.S. Code Cong. & Ad. News 2811, 2813. Second generation statutes, however, can discourage tender offers. See supra note 85 and accompanying text. Discouraging tender offers is contrary to congressional policy. Three Justices stated in MITE Corp. that the states could not frustrate federal policy through local statutes. See Edgar v. MITE Corp., 457 U.S. 624, 630-40 (1982) (plurality opinion of White, J.) (White, J. joined by Burger, C.J., and Blackmun, J.). Second generation statutes violate the supremacy clause because they do not protect investors. Many of these laws hurt shareholders by depriving them of an opportunity to tender their shares at a premium above the market price. "Congress . . . did not want to deny shareholders 'the opportunities which result from the competitive bidding for a block of stock of a given company,' namely, the opportunity to sell shares for a premium over their market price." Id. at 633 n.9 (plurality opinion of White, J.) (quoting 113 Cong. Rec. 24,666 (1967) (remarks of Sen. Javits)).

134. Restrictive business combination provisions will prevent offerors who need the target's assets to finance the purchase of shares from making successful takeovers. See supra note 85 and accompanying text. See infra note 152.


136. This is the MITE Corp. majority's analysis. A state has no legitimate interest in protecting nonresident shareholders. The state gets no benefit from prohibiting a tender offer outside its borders. If a local statute prohibits transactions between nonresidents, the Pike balance will come out against the state. See Edgar v. MITE Corp., 457 U.S. 624, 643-44 (1982). See supra note 72.
activities. State laws that promote a legitimate public interest and regulate commerce only incidentally are valid unless they excessively burden interstate commerce. Statutes that interfere with or that prevent transactions between out-of-state residents are invalid because, although they may promote a local interest, these regulations needlessly burden interstate commerce. States must pursue local goals by means that least affect interstate commerce.

Local governments have a legitimate interest in protecting resident investors and in regulating the internal affairs of domestic corporations. Courts have also accepted as legitimate the states' interest in having benevolent management heading resident corporations. This raises the question of whether local legislations can seek the benefits of benevolent management through restrictive takeover statutes.

The answer is no. As noted, citing a legitimate interest is not enough to pass commerce clause muster. A law must provide benefits to the state. If an organization's management has a particular expertise or social policy that a state finds valuable, protecting that management from a takeover will not ensure that the corporation will continue to behave in the same way. Policy shifts or internal personnel changes can bring new management, new ideas and an end to the benefits that the prior managers bestowed on the state.

137. Cardiff Acquisitions, Inc. v. Hatch, 751 F.2d 906, 909-10 (8th Cir. 1984). States have no legitimate interest in protecting nonresident shareholders. Edgar v. MITE Corp., 457 U.S. 624, 644 (1982). Therefore, insofar as a state statute burdens out-of-state transactions there is no benefit to the state to sustain the law. Id. Statutes that only affect local residents avoid burdens on interstate commerce and protect local investors. See supra notes 135, 136.

138. See supra notes 135-137.

139. "The extent of the burden [on interstate commerce] that will be tolerated will of course depend on... whether [the state's interest] could be promoted as well with a lesser impact on interstate activities." Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970); see Great Atl. & Pac. Tea Co. v. Cottrell, 424 U.S. 366, 372 (1976) (quoting Pike, 397 U.S. at 142).


143. In the commerce clause analysis, the court balances the burdens a statute places on interstate commerce against the actual benefits to the state, not the interest the state is trying to promote. APL Ltd. Partnership v. Van Dusen Air, Inc., [1985-86 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 92,331, at 92,190 (D. Minn. 1985). If a statute is designed to protect local investors—a legitimate local interest—but fails to do so, no benefits will accrue to the state and the law will fail to pass the Pike test. See supra notes 72, 76 and accompanying text.
Furthermore, local governments must promote legitimate interests in ways that have the least affect on interstate commerce. Preventing takeovers is not the most efficient way to foster benevolent management. States can set minimum competency standards for local management. For example, if a state had an interest in having expert management running the local utility company, implementing minimum competency standards would guarantee that whomever was in charge of the company would have the requisite expertise for the job. Local legislators can force resident corporations to implement environmental programs and can encourage social programs with tax incentives. Preventing takeovers only hurts local investors by removing some of the inducement for incumbent management to perform efficiently. Also, laws that protect corporations from takeovers will face supremacy clause problems.

Local legislators can only regulate tender offers for corporations that are closely tied to the state. Local lawmakers must define "target company" narrowly to include only corporations that have a close nexus with the state. The close connection requirement prevents states from exercising jurisdiction over takeovers that they have no legitimate interest in regulating. If the target does not have a strong link with the state, a successful takeover will not have the kind of results that are important to local residents. For example, if the acquirer liquidates a "foreign" corporation, the state would not lose a significant number of jobs or substantial revenue. Therefore, a successful tender offer would have no effects worth disclosing to state residents. The close connection requirement also minimizes potential burdens on interstate commerce by preventing several states from exercising jurisdiction over a single tender offer.

The required connection exists only when the target company has substantial assets in the state and local residents hold a "large" percentage of the target's shares. The percentage of a company's share state resi-
dents hold must only be large when considering the number of shares outstanding and the percentage held by investors in other states. For example, if New York residents hold five percent of the shares in XYZ corporation, and that five percent represents a large number of the outstanding shares, New York could regulate a takeover for XYZ Corp. provided that residents of no other state owned a substantially higher percentage of the company's stock.

A state's interest in protecting local investors is more clearly implicated when its residents hold a large percentage of the target's securities. Moreover, successful offerors often must use the assets of the captured corporation to finance the takeover. Local investors should have an opportunity to consider the effects of such sales on their state before deciding to tender their shares. For instance, if a successful takeover would mean a loss of jobs or tax revenue for the state, resident investors might not want to tender their shares.

A strong nexus will help avoid commerce clause problems. Laws limited in scope to local corporations with close ties to the state fare well under the commerce clause analysis. They do not directly regulate interstate commerce.

If a state law indirectly regulates interstate commerce, the courts will screen it under the *Pike* test. If the target has a large percentage of investors and substantial assets in the state, the presence of a legitimate local interest is clear. If the scope of the statute is limited to local residents, the burden on interstate commerce is not excessive. Target companies must have a large percentage of local investors and assets before state tender offer legislation can constitutionally apply to them.

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151. This would avoid the problem presented by the Illinois statute in *Edgar v. MITE Corp.*, 457 U.S. 624, 645 (1982) (statute regulating takeovers that did not involve a single state resident). See *supra* note 147.

152. *Pinto*, *supra* note 85, at 30, col. 2.

153. *See* *Cardiff Acquisitions, Inc. v. Hatch*, 751 F.2d 906, 911-12 (8th Cir. 1984) (these statutes promote local interests while having minimal effects on interstate commerce). See *supra* notes 147, 149.


If an offeror does not comply with a state provision the state can suspend the offer, but only to its residents. States have no power to suspend an offer to residents of another jurisdiction. A state receives no benefit from protecting investors in other states. Suspending an offer to out-of-state residents puts an excessive burden on interstate commerce and tilts the Pike balance against the regulating state.

Local legislatures can draft effective takeover statutes if these laws apply only to tender offers for state corporations to local residents. States cannot protect incumbent management, by blocking tender offers on a national level, and stay within the bounds of the commerce clause.

CONCLUSION

States can regulate tender offers but not in a manner contrary to the Williams Act or the commerce clause. Local legislatures can protect resident investors. They cannot shield corporations from nationwide takeovers. Any statute that discourages tender offers is subject to preemption. State statutes that give local authorities the power to suspend offers on a national level violate the commerce clause.

There is room for the states to regulate tender offers but any regulation must be in accordance with federal policy and the commerce clause. For example, states can require offerors to disclose information in addition to that required under the Williams Act. The information must be helpful to local investors deciding whether to accept the tender offer. Disclosures that confuse the shareholder or that are excessively burdensome to the offeror defeat the purpose of the Williams Act. If the offeror fails to comply with state law, local authorities can suspend the offer in the state until the bidder satisfies the statutory obligations.

Michael A. McIntosh

157. Id.
158. Cardiff Acquisitions, Inc. v. Hatch, 751 F.2d 906, 911 (8th Cir. 1984); see Edgar v. MITE Corp., 457 U.S. 624, 643 (1982). In MITE Corp. the statute at issue affected investors outside the state. It failed to pass commerce clause scrutiny. Id. at 644-46. The statute challenged in Cardiff allowed the Commissioner to suspend an offer only to state residents if the offeror failed to comply with it. The court upheld the law. Cardiff Acquisitions, 751 F.2d at 911.