

STATE ANTI-TAKEOVER LAWS COMPLICATE ACQUISITION INVOLVING PUBLIC COMPANY

By William S. Skinner, Esq.

The recent resurgence of the tender offer as a technique for friendly corporate acquisitions forces companies and advisors to dust off old “hostile takeover” laws to avoid being tripped up

In the 1980’s heyday of hostile takeovers, state legislatures sympathetic to hometown employers acted to validate a number of defensive tactics (e.g., poison pills and supermajority voting requirements) to protect their domestic corporations. These statutes overruled decisions from courts antagonistic to certain “anti-democratic” takeover defenses. The defensive tactics were intended to force corporate raiders to negotiate with a target corporation’s board and to treat all shareholders fairly in the takeover process.

Many states took protective efforts a step further, though, not only allowing corporations to adopt effective defensive strategies, but imposing self-operative laws that would legally disable a corporate acquirer from voting shares or engaging in transactions with the target (such as a back-end, cash-out merger), unless specified safeguards were observed.

Business Combinations

For instance, Delaware, New Jersey and Pennsylvania all have “business combination” statutes which make life painful for an unwelcome suitor. Unless a transaction has prior approval of the target’s board of directors, a shareholder who newly acquires stock of a public company above a certain threshold (10 percent or 15 percent in these states) is prohibited from merging (among other prohibited transactions) with the target company for a number of years. The goal of any tender offeror is to acquire a majority of the stock via the tender offer, and then conduct a cash-out merger to eliminate the remaining minority shareholders. With the back-end merger prohibited (e.g., for five years in New Jersey), the “raider” is stuck with the unwelcome prospect of coexisting with a substantial minority shareholder population and the ongoing constraints, risks and costs of doing business as a public company.

Control Shares

An additional approach under the Pennsylvania Business Corporation Law is to cancel the voting rights of shares held by an uninvited acquirer of shares, creating another barrier to the acquirer’s control of the company or taking it private.

Consistent with their goal to force the acquirer to negotiate with the board, these defensive statutes typically provide an exemption for acquisitions that are approved in advance by the target’s (pre-acquisition) board. **Early consideration of these rules with experienced local counsel is critical!**

- What to approve? Pennsylvania and Delaware generally allow the board to exempt the transaction from the “business combination” law by approving either the specific “business combination” or the initial share acquisition by the acquirer. In New Jersey, the board must approve the **business combination** before the “stock acquisition date.” Thus, the back-end transaction must be defined and approved before stock is acquired, and may not later be substantially changed.
- When to approve? Generally, the board action must be undertaken before the “stock acquisition date” of the acquirer. Attribution of “beneficial ownership” to shares that are the subject of arrangements or contracts regarding acquisition or voting may have unexpected results! If an acquirer enters into a share purchase agreement with a major shareholder, it may already be too late to get the board’s approval.
- When is board’s approval not enough? Some of Pennsylvania’s anti-takeover provisions are especially prone to unintended – and irremediable – consequences. The Commonwealth’s law has two powerful provisions that do not contain an opt-out provision allowing a board to approve a specific favorable transaction: (i) a “control transaction” law that gives remaining shareholders an appraisal

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remedy at the expense of the acquirer, and (ii) a “control shares” law that voids the acquirer’s voting rights. Unless the corporate charter is amended in advance, a tender offeror will need to obtain shareholder approval at a shareholder meeting in order to restore those voting rights, which, in turn, are necessary to conclude the merger.

The use of a tender offer has the ability to speed up a friendly going-private transaction, but it is important to consider very early in the transaction planning the framework of the applicable state law.



William S. Skinner is a member of the Business & Corporate Practice Group, and concentrates his practice in business and financial matters. He has extensive experience representing clients in the acquisition and sale of businesses, complex debt and equity financing transactions and securities offerings. His clients include developers of commercial real estate, investors, trade organizations and commercial enterprises in a variety of industries. Please contact him at william.skinner@flastergreenberg.com; or 856.661.2262.