Challenges to State Takeover Laws: Preemption and the Commerce Clause

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COMMENTS

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I. INTRODUCTION

With increasing regularity corporations are purchasing each other. To fend off hostile attacks target management has sought the protections afforded by state takeover laws. These statutes delay the takeover, often frustrating the attempt, in contravention of the purposes of the federal rules which view takeovers as an effective way of removing inefficient management. For this reason raiding corporations have sought to enjoin the enforcement of state takeover laws as being preempted by the federal scheme. Additionally, the raiding corporations protest that the extra-territorial effect of the state statutes causes an impermissible burden on interstate commerce. Because of the jurisdictional reach of the state statutes a raiding corporation is often forced to comply with three or four state statutes.

The continued validity of the state regulation of corporate takeovers is questionable as two recent court of appeals decisions suggest.

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sions have struck down anti-takeover laws in New Jersey\textsuperscript{2} and Illinois.\textsuperscript{3} Both of the courts agree that the attempt to regulate tender offers, as embodied in the statutes in question, was preempted by the federal regulatory scheme commonly referred to as the Williams Act.\textsuperscript{4} This Comment will analyze the preemption issue as it relates to state anti-takeover laws, especially in Wisconsin. It will then address those commerce clause problems closely associated with state regulation. First, the Comment will describe the setting in which a tender offer is made to assist in analyzing the conflicting interests in tender offer regulation with respect to the federal and state government.\textsuperscript{5}

II. BACKGROUND OF TENDER OFFER REGULATION

One's view of a hostile cash tender offer\textsuperscript{6} is in large part


5. See F. Deguire, Address of Frank C. Deguire at the Marquette University Law School, March 8, 1979: The Pabst Brewing Company Defends a Takeover Attempt Made by APL Corporation (transcript is on file in the Marquette Law Review). Mr. Deguire was the Chairman of the Board at Pabst while it successfully defended against a takeover bid by APL Corporation. Mr. Deguire's remarks are extremely useful as a gauge of corporate management's sentiments towards a hostile takeover.

6. While the Williams Act does not define the term tender offer, several attempts have been made. See E. ARANOW & H. EINHORN, TENDER OFFERS FOR CORPORATE CONTROL (1973); Note, The Developing Meaning of "Tender Offer" Under the Securities Exchange Act of 1934, 86 Harv. L. Rev. 1250, 1251-54 (1973); S. Rep. No. 550, 90th Cong., 1st Sess. 2 (1967). The American Law Institute suggests the following definition:

TENDER OFFER—(A) GENERAL.—"Tender offer" means an offer to buy a security, or a solicitation of an offer to sell a security, that is directed to more than thirty-five persons, unless—(i) it is incidental to the execution of a buy order by a broker, or to a purchase by a dealer, who performs no more than the usual function of a broker or dealer, or (II) does no more than state an intention to make such an offer or solicitation; and (ii) it satisfies any additional conditions that the Commission imposes by rule.
determined by his position. While incumbent management views the attempt as a raid (with it as the "target"), the offering company prefers to use a more neutral description referring to itself as an "offeror." This language reflects how traumatic the takeover experience is for corporate management.  

To fend off the attack incumbent management often attempts to find a more suitable corporation, referred to as a "white knight," to effect a takeover. Such a move was made by Harnischfeger when faced with a takeover attempt by Paccar. While both takeovers were eventually unsuccessful, Harnischfeger found a company more to its liking, Mannesmann, to make a more lucrative offer.  

A second, and more effective, method of defense is the initiation of preventive actions in anticipation of a takeover. Thus, a corporation makes itself unattractive to a potential offeror by taking anticipatory defensive measures known as "shark repellant." Today, the main targets of tender offers are easily recognizable. Usually one or more of the following conditions exist: stock price lower than book value; a low price to earnings ratio; a small proportion of stock in officers' and di-

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In describing a three day seminar titled "Repelling Corporate Takeovers: A special three day course in the strategies and tactics of resisting corporate raids and preserving business independence" the Dean of the University of Santa Clara Law School writes:

War used to be a simple concept . . . not pleasant . . . just simple. It used to conjure up heroic images of physical battle . . . men of courage and daring risking their lives for principle or profit.

. . . .

What we are concerned with is a type of economic war. Just as many physical wars result from a coveting of one nation by another, so do these economic wars stem from one corporation's desire to acquire another. And when this happens, you've got the ingredients for a corporate takeover battle.

The cover of the brochure for the seminar shows a full-scale medieval battle complete with castles, knights in shining armor, catapults, spears and arrows. (Copy on file in the Marquette Law Review).

rectors' hands; high liquidity and low debt/equity ratio; excess, hidden, understated or undervalued assets; weak or timid management; or poor stock market performance. 9 When faced with such a situation incumbent management, toward off a future takeover bid, has a number of shark repellant options. Measures such as amending the articles of incorporation to raise voting requirements for mergers or acquisitions, reincorporating in a state with a delaying takeover statute, requiring that directors only be removed for cause, staggering directorships and raising quorum requirements are usually readily available under the corporation law of the state of incorporation. 10 In addition, inserting a super majority provision in the articles of incorporation for the approval of any tender offer similarly discourages potential takeovers. Purchasing a highly regulated corporation, such as a trucking firm, would also delay the offer until approval could be obtained from the regulatory agency. Similarly, the purchase of a firm that competes with a raider would create antitrust barriers to such a merger. 11 However, these defensive maneuvers have come under attack by the pro-takeover SEC. 12 As evidence of this position, the SEC has required that corporations disclose shark repellant amendments in their proxy statements to shareholders. 13 While many of the defensive moves suggested above are not necessarily tied to repelling takeovers, the SEC has taken the position that it will review all measures "designed to make the subject company unattractive as a potential target." 14 State takeover laws operate within this combative framework.

One more actor must be included to make the picture complete. The "arbitrageur" is a person (or firm) who takes advantage of disparate prices of the same security in different marketplaces. The arbitrageur buys stock from nontendering

10. Id. at 14.
11. Id.
12. Leiman, Recent Developments in Tender Offers: Defensive Tactics, in PLI, Tenth Annual Institute on Securities Regulation 289 (A. Fleischer, M. Lipton and R. Stevenson eds. 1979) [hereinafter cited as Leiman].
14. Id. at 80,985.
shareholders at a price slightly below the tender price and then tenders the shares himself in order to secure his profit.\textsuperscript{15} Thus, the shareholder insures a high price for his shares even if the tender offer is not completed, totally avoiding any of the risks associated with holding stock which would later fall in price if the tender offer fails.\textsuperscript{16} The existence of the arbitrageur forces incumbent management to represent two diverse sets of shareholders. Target management is placed in a no win situation. Investors who do not tender their shares demonstrate their confidence in present management along with a desire for long term investment. On the other hand, the arbitrageur shareholder seeks rapid profit, and wants the tender offer to be completed.\textsuperscript{17}

Within the tender offer framework outlined above, federal and state legislation has taken divergent paths. This divergence, the SEC\textsuperscript{18} and most commentators\textsuperscript{19} suggest, preempts

\textsuperscript{15} Johnson, Disclosure in Tender Offer Transactions: The Dice Are Still Loaded, 42 U. Pitt. L. Rev. 1, 2 n.5 (1980).


\textsuperscript{17} Stavrow, supra note 16, at 12. Even the losers in the takeover game can make money. The raiding company usually owns a large block of target company stock purchased in anticipation of the tender offer. After the raider is rebuffed by target management, usually during negotiations to accomplish a merger or a friendly takeover, the raider may offer the shares to the target at a premium. These transactions have been referred to as "corporate kidnapping," or "extortion." See Blustein, More Firms Paying Premium Prices to Wrest Shares From Antagonists, Wall St. J., Jan. 8, 1981, at 21, col. 4; Fortune, May 8, 1978, at 91.

\textsuperscript{18} See 44 Fed. Reg. 70,329 (1979). The comments of the SEC which accompanied the newly adopted regulations for tender offers stated:

Rule 14d-2(b) is intended to prevent public announcements by a bidder of the material terms of its tender offer in advance of the offer's formal commencement. The Commission believes that this practice is detrimental to the interests of investors and results in many of the abuses the Williams Act was enacted to prevent.

the state regulation. While the legislative intent of the Williams Act suggests neutrality, intending to neither favor nor disfavor tender offers,20 many have viewed the SEC as having a strong pro-takeover bias.21 State statutes, on the other hand, generally improve incumbent management's position by furnishing them with a tool, delay, often considered fatal to a tender offer.22

III. THE WILLIAMS ACT

In response to the growing number of tender offers23 Congress enacted the Williams Act.24 Congress was concerned with affording shareholders protection from hostile takeovers.25 The Supreme Court, in reviewing the legislative history of the Act, stated: "[t]he purpose of the Williams Act is to insure that public shareholders who are confronted by a cash tender offer for their stock will not be required to respond without adequate information regarding the qualifications and intentions of the offering party."26 The Act has a two-fold purpose. First, Congress designed the law to insure that investors were well informed, and second, Congress in-

Act). But see The Constitutionality of State Takeover Statutes: A Response to Great Western, 53 N.Y.U. L. Rev. 872 (1978) and Note, Securities Law and the Constitution: State Tender Offer Statutes Reconsidered, 88 Yale L.J. 510 (1979) (State statutes should not be preempted by the Williams Act). Wilner & Landy argue that the state statutes are preempted principally because the advance notice and hearing requirements frustrate the purpose of the Williams Act. Additionally, they argue there is pervasive federal regulation in the tender offer area and that certain takeover provisions, particularly withdrawal and proration provisions, are in direct conflict with the Williams Act. Wilner & Landy, supra note 19, at 23-32.

23. The number of tender offers increased from 8 to 107 in the six years between 1960 and 1966. The number of tender offers peaked in 1968 at 139. In 1970 they declined to 34 but by 1978 there were over 100. See 111 Cong. Rec. 24662-64 (1967); Jarrell & Bradley, The Economic Effects of Federal and State Regulations of Cash Tender Offers, 23 J.L. & Econ. 371, 400 (1980).
tended the law to favor neither the offeror nor the target.\textsuperscript{27} The mechanics of the Act require a person or corporation that acquires five percent or more of any class of equity securities of a registered company to file a Schedule 13D with both the SEC and the target company.\textsuperscript{28} This filing must occur within ten days after the five percent ownership level has been reached.\textsuperscript{29} Among other things, the offeror must disclose the amount and source of the funds for the purchase, his identity and the extent of his holdings in the company.\textsuperscript{30} In addition, any plans the offeror might have for major changes in the structure or operations of the target, such as plans to liquidate the target, sell its assets or merge it with another company, must also be disclosed.\textsuperscript{31}

Additionally, section 14(d) of the Exchange Act provides that those required to file under section 13(d) must also file any solicitation materials prepared in connection with the tender offer with the SEC.\textsuperscript{32} This 14(d)-1 statement provides for the additional disclosure of such things as the offeror's past transaction with the company,\textsuperscript{33} and any other material financial information about the offeror.\textsuperscript{34} The material facts required to be disclosed include any possible antitrust or legal conflicts which might arise as a result of the tender offer.\textsuperscript{35} The relevant facts set forth in the Schedule 14D-1 are sent to both the target company and its shareholders simultaneously.\textsuperscript{36}

The filing and disclosure requirements are just a part of the Williams Act. In addition, there are several substantive provisions which provide protection to target company shareholders. First, the shareholder is provided with a seven-day withdrawal period after receipt of the offer.\textsuperscript{37} The shareholder

\textsuperscript{28} 15 U.S.C. § 78m(d) (1976).
\textsuperscript{29} \textit{Id}.
\textsuperscript{30} \textit{Id}.
\textsuperscript{31} \textit{Id}.
\textsuperscript{33} \textit{Id}.
\textsuperscript{34} 17 C.F.R. § 240.14d-1 (1979).
\textsuperscript{35} \textit{See} 17 C.F.R. § 240.14d-100(5) (1979).
may similarly withdraw if after sixty days from the date of the original tender offer the offeror has not purchased the shares. Second, when the number of shares tendered is greater than the number of shares originally sought, the offeror is required to purchase the shares tendered in the first ten days of the offer, on a pro rata basis. Third, any change in the terms of the offer, such as an increase in the purchase price, applies to all of the shareholders even after they have tendered their shares. Finally, the Act also contains a broad anti-fraud provision.

Effective January 7, 1980, the SEC promulgated new rules pertaining to tender offers. In the words of the Commission, the new rules are designed to "implement existing statutory requirements by providing specific filing, delivery and disclosure requirements, optional dissemination provisions and additional substantive regulatory protections." Especially important in light of state regulation is rule 14d-2 which establishes the criteria for commencement of tender offers. The rule provides that a public announcement by an offeror through a press release, newspaper advertisement or public statement will constitute the commencement of a cash tender offer, provided further that the statement include the identity of both the offeror and the target company, the amount and class of securities being sought and the price or range of prices being offered.

This new rule is expressly designed to prevent public announcements of the tender offer's material terms prior to the offer's formal commencement. Many of the state takeover statutes had specifically provided for a precommencement no-

38. Commencement of the tender offer is measured from the date of filing the Schedule 14D-1 with the SEC. See 15 U.S.C. § 78n(d) (1976).
42. 15 U.S.C. § 78n(e) (1976). It is not yet settled whether a private right of action exists under this section. For a general discussion of this problem see Note, Standing Under Section 14(e) of the Securities Exchange Act of 1934: May a Tender Offeror Sue for Injunctive Relief, 8 FORDHAM URB. L.J. 405 (1979-80).
45. Id. at 70,328.
tification period. While the Commission stated that the purpose of prohibiting precommencement public announcements was for the protection of shareholders, it is clear that such a provision will reinforce the SEC's position that state regulation in the tender offer area is preempted.

In promulgating such regulations the SEC relied upon its perception of the legislative intent behind the Williams Act. Both the Senate and House reports accompanying the Williams Act state:

Without knowledge of who the bidder is and what he plans to do, the shareholder cannot reach an informed decision. He is forced to take a chance. For no matter what he does, he does it without adequate information to enable him to decide rationally what is the best possible course of action. This is precisely the kind of dilemma which our security laws are designed to prevent.

Precommencement notification forces a shareholder to respond to the offer without full and adequate information. Further, such an announcement will probably trigger arbitrageur activity resulting in volatile disruptions in the price for which the shares are traded. It is felt that rule 14d-2 will help to eliminate this arbitrage activity, which in turn will benefit target company shareholders.

Generally, the new rules are designed to protect the shareholder of the target company. For example, the target company is required to publish a statement disclosing its position with respect to the tender offer. The target must either accept or reject the offer, express no opinion and assure neutrality toward the offer, or state that it is unable to express an opinion toward the offer. This information is part of the

48. See, e.g., HAWAII REV. STAT. § 417E-3(F) (1976).
54. Id. See also 44 Fed. Reg. 70,338-9 (1979).
new Schedule 14D-9 which the target company must file as soon as practicable after the date the company's position is first announced to its shareholders. The additional information required in the Schedule 14D-9 greatly expands the scope of the disclosure required of the target company. Certain negotiations and transactions by the target company, any actual or potential conflicts of interest and such additional information as may be necessary to keep the shareholders informed must be included in the Schedule 14D-9. If any material changes in the tender offer occur, the target is also required to amend the Schedule 14D-9 in a manner reasonably designed to inform the shareholders of such change.

In Canadian Pacific Enterprises, Inc. v. Krouse, the validity of SEC rule 14d-2 was challenged. An Ohio statute prevented an offeror, in this case Canadian Pacific, from making its offer until at least twenty days after public announcement of the terms. Canadian Pacific successfully argued that it was impossible to comply with the twenty-day provision in the Ohio statute, given the five-day provision in rule 14d-2. Having publicly announced the identities of the offeror and the target, the amount and class of securities sought, and the price, Canadian Pacific was required by 14d-2 to commence or withdraw its offer within five business days of the announcement. The Ohio twenty-day rule would prohibit Canadian Pacific from making its offer within the federally mandated period.

The Southern District of Ohio had already decided in AMCA International Corp. v. Krouse that the Williams Act

57. Prior to the adoption of these rules the target company was under no obligation to disclose anything. 17 C.F.R. § 240.14d-1-4, 100 (1976).
did not preempt the Ohio Act. However, the AMCA court took judicial notice of pending rule 14d-2(b), stating, "the Ohio Act in its present form will indisputably be preempted when the new federal regulation becomes effective." This statement was based upon the Supreme Court pronouncement in *Florida Avocado Growers v. Paul,* where the court held that the federal exclusion of state law is inescapable where it is physically impossible to comply with both.

The court in *Canadian Pacific Enterprises* took a two-step approach in analyzing the validity of the new rules. First, the court reviewed the statutory authority relied on by the SEC in promulgating rule 14d-2 to decide whether, taken individually and collectively, these sections authorize the SEC to prescribe the timing of announcement and filing relative to the making of a tender offer. Then, the court relied on the standard of review for formal rulemaking found in the Administrative Procedure Act to determine whether the SEC exceeded its agency authority in promulgating rule 14d-2.

This is a crucial battle for proponents of state regulation. If rule 14d-2 is a valid exercise of agency authority and the SEC satisfies the arbitrary and capricious test of section 706 of the Administrative Procedure Act, a court need only resort to an analysis of the clear physical preemption of the state laws without any inquiry into the purposes of the federal or state legislation. This argument is enhanced by the SEC's position that it is not the commencement date alone which conflicts with the State regulation. All of the time periods in the Williams Act, minimum periods, withdrawal and pro rata rights, and best price, are keyed into the commencement

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64. *Id.* at 933-34.
67. *Id.* at 142-43.
68. See 44 Fed. Reg. 70,326 (1979). The following sections of the Exchange Act were relied on: 3(b), 14(d), 14(e) and 23(a).
Thus, any state statute which deviates from the time schedule established in rule 14d-2 would be preempted, and every state statute in one way or another delays the tender offer process.72

Each of the four sections relied on by the SEC in promulgating the new rules needs to be examined. First, section 3(b) of the Exchange Act provides that “[t]he Commission . . . shall have the power by rules and regulations to define technical, trade, accounting, and other terms used in this chapter, consistently with the provisions and purposes of this chapter.”73 While the Williams Act does not use the term commencement, nor is it found anywhere in the Exchange Act, the Canadian Pacific court held that the term defines a technical term, and is a key concept of the Act. Specifically, section 14(d)(1) of the Act74 provides that it is unlawful to make a tender offer unless, at the time the offer is made, copies are first sent to shareholders. However, the court failed to note that commencement provisions involve much more than the simple setting of a date. The commencement provisions also include substantial disclosure requirements to insure uniformity and shareholder protection. Indeed, the disclosure requirements appear to have been selected to insure that they would conflict with the federal rules.

Section 23(a) of the Exchange Act75 probably provides a much sounder basis for the regulation. This section gives a broad, general rulemaking authority to the SEC, “to make such rules as may be necessary or appropriate to carry out the provisions of this chapter . . . .”76 The Supreme Court has consistently held that regulations promulgated under such sections will be sustained so long as they are “reasonably related to the purposes of the enabling legislation.”77 As discussed above, the purpose of rule 14d-2 is to further share-
holder protection and maintain the stated neutrality between the target and the offeror set forth in the Williams Act. The establishment of a commencement date clearly furthers this purpose.

The final two sections of the Exchange Act relied on by the SEC, 14(d)(4) and 14(e), both involve substantive protections designed to regulate the conduct of those involved in tender offers, and especially protect against fraud and other manipulative behavior. The establishment of a commencement date by the SEC is especially competent within the meaning of these two sections, due to the arbitrage activity associated with the commencement of a tender offer. Un sophisticated shareholders are easily taken advantage of as the price of the shares becomes volatile. However, while the commencement criteria in rule 14d-2 does provide for some minimum protections to shareholders faced with this dilemma, state statutes go much further. This is especially true in states like Wisconsin which provide for a hearing before the Commissioner of Securities to determine the fairness of the offer. Since the Williams Act is a minimum disclosure statute, it might be argued that state statutes can go further in the protection of shareholders.

Upon completing this analysis the district court in Canadian Pacific Enterprises determined that the promulgation of rule 14d-2 was abundantly authorized by the enabling sections. Undertaking a narrow review of the regulation under the arbitrary and capricious standard the court then held that the regulations were reasonably related to the purposes of the Williams Act as expressed in the legislative history. Moreover, the court recognized that the delays incumbent in state regulation were designed to aid the target company management, in express contravention of the neutrality of the Williams Act. The purpose of the Williams Act, to protect investors, would be frustrated by state efforts to provide a

80. Wilner & Landy, supra note 19, at 10; Preempting the Maze, supra note 7, at 860.
81. Wis Stat. § 552.05 (1979).
defensive tactic to target companies. Applying the arbitrary and capricious standard, the court found that the findings of the SEC were based upon a rational foundation. The court specifically rejected the argument that the SEC sought preemption solely for the sake of preemption. Even if this were the case, the court felt that the rulemaking process itself was neither arbitrary nor capricious. The purpose for the regulation is not controlling as long as the Commission did not act in an arbitrary or capricious manner in promulgating the rule.

The SEC, through its rulemaking power, is not alone in attacking the validity of state takeover laws. Three circuit courts have reviewed state takeover statutes and all three have held that the statutes in question were preempted. Prior to analyzing those decisions, a brief review of the structure of the state takeover laws will be presented.

IV. THE COMPOSITION OF STATE TAKEOVER LAWS

In 1968 when the Williams Act was enacted, only Virginia had a takeover statute and its statute had never been enforced. When the Williams Act was amended in 1970, two additional states, Ohio and Nevada, had passed takeover laws. However, when the amendments to the Williams Act were considered, none of these state statutes had ever been used. From the silence in the legislative history, it is apparent that Congress was unaware of the state regulation in the area.

State statutes vary considerably in their specific provisions, although a number of common trends can be identified. First, the jurisdictional provisions are based on the re-

83. Id. at 90,357.
84. Id.
86. VA. CODE § 13.1-5.28. The Virginia statute was enacted four months prior to the Williams Act.
87. OHIO REV. CODE ANN. § 1707.041; Nev. REV. STAT. § 78.376-.3778.
relationship between the target corporation and the state. A combination of factors is used to determine this relationship: (1) the target's state of incorporation; (2) its principal place of business; or (3) the location of substantial assets. The extraterritorial effect of the state statutes has resulted in a number of cases where more than one state has attempted to regulate the takeover.

The jurisdictional requirements, and their extraterritorial effect, are but one of the problems with state regulation. In addition, state laws generally require the offeror to file more extensive disclosures with both the target management and the state securities commission, usually in advance of the actual offer. Thus, the resulting delay of administrative procedures gives the target management a great deal of flexibility in defending against the takeover.

While several regulatory approaches are taken by each state, often in combination, there are a number of recurring themes. First, a number of states have provisions similar to the Ohio statute, which provides for precommencement notification. Typically, the disclosure statement necessary for

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91. All states rely on this jurisdictional provision.


94. A most recent example of this problem arose when Seagram Company announced a $2.03 billion tender offer for St. Joe Minerals Corporation, the largest producer of lead in the United States. The management of St. Joe's rejected the $45 per share offer as too low. Sensing a fight, Seagrams sought injunctions to have the New York and Nebraska takeover laws declared invalid. Additionally, Seagrams stated it was prepared to fight the Missouri and Louisiana statutes which were also applicable. See Wall St. J., Mar. 12, 1981, § 1, at 3, col. 1.

95. State laws generally require more disclosure than is required in Schedule 13-D, although in some states a copy of the Schedule 13-D is sufficient. See, e.g., Wis. Stat. § 552.03(2) (1979).


97. See the discussion accompanying notes 60-67 supra.
precommencement notification contains the elements of commencement in rule 14d-2. 98

Second, state laws generally require that the offeror hold tender offers open for longer than the ten-day federal period. For example, Massachusetts and Michigan force the tender offer to be held open for at least sixty days. 99 In addition, states usually provide for liberal withdrawal rights, which effectively extend the tender offer period. 100

Perhaps the most important feature of the state anti-takeover laws is the provision for administrative review. If the target is within the jurisdictional reach of the state (usually it will be within the reach of more than one state) 101 a hearing can be requested by the target with the state’s securities commission. 102 The Illinois statute invalidated in Mite Corp. v. Dixon is representative of the various states’ review sections. In fact, the Wisconsin statutes were almost identical to the Illinois statute. The Wisconsin statutes have since been amended, although it is not clear that the revisions will pass constitutional review unscathed. Generally, these review provisions contain the following elements. The commissioner, in his own discretion, may require that the offeror file any other additional information which the commissioner deems material to the takeover. 103 If the commissioner is dissatisfied with the offeror’s disclosure, in that it does not contain all the information required or does not provide full disclosure to shareholders of all material information covering the offer, the commissioner may, by order, summarily delay the offer. 104 In addition, the commissioner is empowered to call a hearing concerning the offer, for the protection of the state’s share-

98. Id.
100. See Jarrell & Bradley, supra note 90, at 378.
101. Of the states that do not regulate takeovers, only California is a major industrial center. The other states without takeover provisions are: Alabama, Arizona, Montana, New Mexico, North Dakota, Oklahoma, Oregon, Rhode Island, Vermont, Washington, West Virginia and Wyoming.
103. Wis. Stat. § 552.05(3) (1979).
104. Id.
If the target company requests a hearing, the commissioner must call one. The statute provides further that, if the commissioner finds that the offer fails to provide for full and fair disclosure to shareholders of all material information concerning the offer, or that the offer is unfair or inequitable to shareholders, the commissioner shall order denial of the registration of the offer. Finally, the commissioner may also seek an injunction against anyone who appears, to the commissioner, to have violated the state's anti-takeover law.

Finally, state takeover statutes generally contain enforcement mechanisms. The state securities commission can often order both cease and desist orders and injunctions. Violations of the statutory provisions can result in a broad range of penalties, such as criminal prosecutions, fines and forfeitures, and civil liability. However, the biggest penalty to the offeror may be the delay which attaches to the administrative process.

While the purpose of the state statutes may be to protect shareholders, there is no doubt that their main effect is the protection of target company management from unfriendly tender offers. It is clear that the hearing provisions and precommencement notification result in substantial delay, to the advantage of the target company. Tender offers may be discouraged as the target organizes its defensive maneuvers. Wilner and Landy argue that these delays result in sizable price fluctuations, which may result in the SEC ordering a halt to the trading of the target's shares.

It is less clear, however, that the delay resulting from the state regulations is not in the best interests of the shareholder-
ers. First, the longer the delay, the more opportunity the target company has to search out a white knight, thereby effecting a more compatible union.\textsuperscript{113} Not only is the price usually higher, but there is also less disruption of management and company operations. This results in a less costly takeover. Moreover, the administrative mechanisms for delay in state regulation may in fact foster the market place competition sought in the Williams Act.\textsuperscript{114} The delay and disclosure requirements allow for more competition in the tender offer market place. The successful offeror will be forced to pay a higher premium in order to outbid the competition resulting from such regulation.\textsuperscript{115} An empirical study has shown a steady increase in the average cash tender price premium,\textsuperscript{116} from 32 percent prior to the Williams Act to nearly 53 percent after its passage.\textsuperscript{117} The study concludes that the effect of state laws has been to increase the average cash tender premium from 53 percent to 73 percent.\textsuperscript{118} Armed with this data, a target company may be able to successfully present a valid legal and economic argument on the validity of state regulation.\textsuperscript{119} However, to date the courts have been more willing to adopt the SEC preemption argument.

V. RECENT DECISIONS AFFECTING THE STATE REGULATION OF TENDER OFFERS

A. Preemption

Raiding corporations urge that state takeover laws are preempted under the supremacy clause of the Constitution.\textsuperscript{120} "No simple formula can capture the complexities of this determination; the conflicts which may develop between state and federal action are as varied as the fields to which congres-

\textsuperscript{113} Boehm, \textit{supra} note 72, at 737.
\textsuperscript{115} Jarrell & Bradley, \textit{supra} note 90, at 373.
\textsuperscript{116} Id. The measure of tender price premium used was the tender price per share divided by the target's share value forty days prior to the offer minus one, after adjustments for stock splits and dividends.
\textsuperscript{117} Id.
\textsuperscript{118} Id.
\textsuperscript{119} See the discussion accompanying notes 153-61, infra.
\textsuperscript{120} U.S. Const., Art. 1, § 10.
sional action may apply." Each case will turn on the peculiar interaction of the state and federal schemes in question, so that prior cases only furnish rough guidelines for the courts to follow. The general test to be followed was summarized by the Supreme Court in Jones v. Rath Packing Co.: The first inquiry is whether Congress, pursuant to its power to regulate commerce, U.S. Const., Art. 1, § 8, has prohibited state regulation of the particular aspects of commerce involved in this case . . . . [W]hen Congress has "unmistakably . . . ordained," Florida Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 132, 142 (1963), that its enactments alone are to regulate a part of commerce, state laws regulating that aspect of commerce must fall. This result is compelled whether Congress' command is explicitly stated in the statute's language or implicitly contained in its structure and purpose. City of Burbank v. Lockheed Air Terminal, Inc., 411 U.S. 624, 633 (1973); [citation omitted]. Congressional enactments that do not exclude all state legislation in the same field nevertheless override state laws with which they conflict. U.S. Const., Art. VI. The criterion for determining whether state and federal laws are so inconsistent that the state law must give way is firmly established in our decisions. Our task is "to determine whether, under the circumstances of this particular case, [the State's] law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." Hines v. Davidowitz, 312 U.S. 52, 67 (1941). Accord, De Canas v. Bica, 424 U.S. 351, 363 (1976); Perez v. Campbell, 402 U.S. 637, 649 (1971); [citation omitted]. This inquiry requires us to consider the relationship between state and federal laws as they are interpreted and applied, not merely as they are written. Congress has not expressly chosen to preempt the states from regulating tender offers. In fact, section 28(a) of the 1934 Exchange Act appears to have a contrary tone. The

123. Mite Corp. v. Dixon, 633 F.2d 486, 490 (7th Cir. 1980).
125. Id. at 525-26.
126. Mite Corp. v. Dixon, 633 F.2d 486 (7th Cir. 1980).
section provides that: "Nothing in this chapter shall affect the jurisdiction of the securities commission . . . of any state over any security or any person insofar as it does not conflict with the provisions of this chapter or the rules and regulations thereunder." It is argued, however, that section 28, being a part of the original Exchange Act in 1934, was designed to preserve state blue sky laws already in existence and has no effect on state regulation of tender offers. As has already been noted, the legislative history of the Williams Act is silent with respect to the question of the preemption of state regulations, as no such regulation was yet in existence.

The Seventh Circuit, in Mite Corp. v. Dixon also rejected an implicit preemption argument. However, at least one commentator has suggested that the Williams Act, coupled with the new SEC rules, presents such a pervasive scheme of federal regulation as to make reasonable the inference that Congress left no room for the states to supplement it. In Mite, the court rejected any attempt to analogize the tender offer regulation field to the facts of City of Burbank v. Lockheed Air Terminal, Inc., the leading implicit preemption case. In City of Burbank, a city curfew of jet flights was held to be preempted by the Noise Control Act of 1972. The Mite court stated that the detailed and comprehensive scheme of federal regulation of aircraft noise that led to preemption in City of Burbank was not present in the Williams Act. Essentially, the court stated the Williams Act is a minimum disclosure act which does not present the same comprehensive scheme found in City of Burbank. This appears to leave the door open to state regulations which, for a legitimate state purpose, would require more extensive disclosure.

Where Congress has legislated in an area of paramount

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130. See Langevoort, supra note 19, at 248. But see Wilner & Landy, supra note 19, at 29.
131. See the discussion accompanying notes 86-88 supra.
132. 633 F.2d 486 (7th Cir. 1980).
133. See Comment, supra note 52, at 931. Contra, Langevoort, supra note 19, at 248.
135. Id. at 633.
136. 633 F.2d at 490.
federal importance, preemption has also been found, even if the federal legislation does not present a pervasive scheme.\textsuperscript{137} In areas such as foreign affairs\textsuperscript{138} and national security\textsuperscript{139} the Supreme Court has held that state statutes were implicitly preempted. Federal securities regulation is not of equivalent paramount concern. "On the contrary, the absence of an exclusive federal interest in the field of securities regulation is persuasively demonstrated by the historically coordinate role of state regulation in the field.\textsuperscript{140}

Thus, in the absence of either explicit or implicit preemption, the issue is whether "[the states'] law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."\textsuperscript{141} Utilizing this rationale, the state takeover laws of eleven states have been preempted.\textsuperscript{142}

The purpose of the Williams Act is crucial under this preemption analysis when determining whether the federal scheme leaves room for state regulation as the courts attempt to balance the competing interests. The dominant theme of the Williams Act is investor protection.\textsuperscript{143} This is essentially achieved through a variety of disclosure provisions, operating

\begin{itemize}
  \item 137. \textit{Id.}
  \item 139. Hines v. Davidowitz, 312 U.S. 52 (1941).
\end{itemize}
under the assumption that the best protection investors can have is information.

The approach the Williams Act takes is referred to as a “market approach.” “The function of federal regulation is to get information to the investor by allowing both the offeror and the incumbent managers of a target company to present fully their arguments and then let the investor decide for himself.” Clearly, those state provisions concerning precommencement notification are void because they are in direct conflict with the Williams Act. It is also urged that provisions of the state statutes which seek additional disclosure and place great discretion in the securities commission are void because of the delay incurred which is inimical to the Williams Act design. Delay is, as we have already seen, the most potent weapon target management has at its disposal.

In *Kennecott Corp. v. Smith*, the Third Circuit Court of Appeals made clear its opposition to such delaying provisions:

The “market approach” for protecting investors established by the Williams Act contemplates the free flow of information from both sides, so that the shareholders can make an unfettered and knowledgeable choice whether to relinquish their shares for a cash premium. When commencement of the offer, which entails distribution of information, is delayed, the market approach cannot be effectuated, because the choice can no longer be an informed one. While the shareholders have yet to receive the benefit of full knowledge of the merits and terms of the challenger’s offer, the target’s management can use the period of delay to send materials to the shareholders in order to discourage them from tendering their stock.

The defensive maneuvers which become available to the target management as a result of the delay take away the shareholder autonomy which the Williams Act is designed to protect. Ancillary effects such as the detrimental effects on the stock market, the possibility of frustrating the eventual success of a tender offer, and the increased cost to the offeror

144. Mite Corp. v. Dixon, 633 F.2d at 492 (quoting Great Western United Corp. v. Kidwell, 577 F.2d 1256, 1276 (5th Cir. 1978)).

who is usually paying interest on money borrowed to complete
the tender offer, all weigh heavily against state efforts to delay
tender offers. In essence, the cumulative impact of the ef-
cfects flowing from delay in the commencement of the offer is
to "disrupt the neutrality essential to the execution and the
proper operation of the market approach for protecting inves-
tors embraced by the Williams Act." Additional arguments were used to strike down the provi-
sions for administrative review and hearings found in the Illi-
nois and South Carolina statutes. These provisions were in
many respects identical to the former Wisconsin provisions
which empower the securities commissioner to hold hearings
on the fairness of the tender offer. The Illinois Act, for ex-
ample, empowers the Secretary of State to pass on the sub-
stantive fairness of the tender offer and to prohibit it from
going forward if the Secretary finds the offer inequitable.
Not only does this create enormous potential for delay, but it
also substitutes the judgment of the reviewing body for that
of the investors. This approach, known as the "benevolent bu-
reaucracy" approach, is fundamentally inconsistent with the
Williams Act purposes. The Williams Act contemplates un-
fettered choice by investors who have been informed as a re-
sult of the disclosure requirements. Both the House and Sen-
ate reports observed that the Williams Act "is designed to
make the relevant facts known so that shareholders have a
fair opportunity to make their decision." Hearing type stat-
utes, therefore, frustrate the express Congressional intent to
allow shareholders to make their own decisions under a mar-
ket approach. Investor protection at the expense of investor
autonomy is a result inconsistent with the federal scheme.
Such substitution of judgment is not tolerable under the Wil-
liams Act.

146. Id. at 98,837.
Rep. (CCH) ¶ 97,804, at 90,032 (D. S.C. Dec. 4, 1980); see also Mite Corp. v. Dixon,
633 F.2d at 495.
148. Wis. Stat. § 552.05(4)-(5) (1979). See also discussion accompanying notes
103-08, supra.
150. Mite Corp. v. Dixon, 633 F.2d at 494.
Cong., 1st Sess. 3 (1967).
The problem with the approach taken by Congress is that, while it expresses a desire to protect investors, it also restricts the ability of target management to seek a better price, thus restricting competition. Studies of price variations in premiums which offerors eventually pay when faced with the possibility of delay indicate a much greater percentage premium. A true market approach would encourage competition and not simply encourage disclosure of information. The problem, however, is that courts are constrained by the legislative purpose, and cannot substitute their judgment for that of Congress.

While contrary to the Williams Act, there may be legitimate state interests in the protection of investors in the tender offer area. Four different concerns have been identified to legitimate state regulation of takeovers:

First, states wish to assure that resident shareholders are given enough time and information to make an informed judgment as to a transaction that is, in substance, a transformation of the corporate structure. Second, takeover legislation may be viewed as an exercise of the states' right to prescribe the attributes of a share of stock in a corporation organized under their laws. Third, to the extent the statute seeks to impede the departure of corporate plant and facilities, it is prompted by economic regulatory considerations. Fourth, to the extent statutes apply to corporations headquartered in the state, it reflects the states' desire to improve the quality of life within their borders.

Three decisions prior to the SEC's promulgation of the new rules validated state takeover statutes relying on the above listed state interests. In AMCA International Corp. v. Krouse, various notice provisions of the Ohio takeover statute and an administrative review provision were viewed as presenting no "obstacle to the accomplishment and execution of the full purposes and objectives of Congress." However, the court's decision in Canadian Pacific Enterprises, Inc. v. Krouse overrules the AMCA decision.
In a similar fashion the Kentucky takeover statute has been held valid in light of the Williams Act. In *Strode v. Esmark*,\(^{168}\) a Kentucky circuit court ruled that Kentucky had a legitimate state interest in regulating the internal affairs of companies having a significant nexus with Kentucky. The court found that it was the expressed intent of Congress, under section 28(a) of the Act, to allow states to regulate takeovers.\(^{169}\) However, because of the direct conflict with Kentucky's notice provisions, the Williams Act probably preempts the Kentucky statute. It is fairly clear that the only purpose of the Kentucky statute is to delay tender offers. There are no additional disclosures of information to shareholders, nor is there a provision for administrative review.

Finally, in *Wylain, Inc. v. TRE Corp.*,\(^{160}\) the court took a somewhat different approach in upholding the Delaware statute over both commerce clause and preemption objections. The Delaware statute did not provide for administrative review, although it did extend the time period of the tender offer. This waiting period was designed to allow stockholders sufficient time to review the information related to the offer. The court held that this short delay imposed no burden on interstate commerce because it did not pose a threat to the successful completion of the offer.\(^{161}\)

In addition, the Delaware Chancery Court held that the Delaware Act was not preempted by the Williams Act. The court responded to the argument that the Delaware Act upset the claimed neutrality of the federal scheme as follows: "True
neutrality means that neither side in tender offer battles should be permitted to deny a stockholder the opportunity to make an informed decision." The Delaware Act simply provided more protection for the investor. Since the Williams Act is a minimum disclosure statute, such additional stockholder protections appear consistent with the federal law. While such an analysis does not have popular support, with the majority of decisions finding preemption, it is persuasive. Investors purchase stock to make money. Delay results in higher premiums paid, and therefore a greater return to the investors. It may be that the best interests of the investors are served in this fashion.

B. Commerce Clause

The final challenge to the validity of state regulation of takeovers arises under the commerce clause. This question need not be reached once the court finds preemption. However, some courts have relied on this analysis, concluding that the state statutes not only are preempted but also violate the commerce clause. The Supreme Court outlined the test to be used in determining whether state legislation impermissibly interferes with or hinders interstate commerce in *Pike v. Bruce Church, Inc.*:

Where the statute regulates even-handedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits [citation omitted]. If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities.

The commerce clause challenge raises the problems attendant to the extraterritorial effect of the state takeover stat-

162. Id. at 349.
163. U.S. CONST. Art. 1, § 8 provides that: "[t]he Congress shall have the power . . . to regulate commerce . . . among the several states."
utes. In *Hi-Shear Industries, Inc. v. Campbell*, South Carolina attempted to enforce its takeover law on a tender offer. Hi-Shear had commenced an offer to purchase Raybestos. Hi-Shear is a Connecticut corporation, with its principal place of business also in Connecticut. Raybestos is a Delaware corporation, with New York as its principal place of business. Raybestos employs about 500 people in South Carolina, bringing it within the state's takeover law, yet less than one percent of all outstanding shares of Raybestos were owned by South Carolina citizens.

The court held that for the South Carolina Act to have such global impact places an impermissible burden on interstate commerce. While South Carolina may have a legitimate local interest in preventing locally managed corporations from being taken over by foreign corporations, the jurisdictional reach of the statute does not so limit its effects. As summarized by the Seventh Circuit in *Mite Corp. v. Dixon* a jurisdictional scheme such as this is not permissible:

The Act's most obvious burdens result from its global impact. Once the Act has been invoked, all purchases, or offers to purchase by the offeror, of the target company's stock pursuant to a tender offer may be halted, including transactions to be executed entirely outside the boundaries of [the state]. The . . . Act thus possesses a significant potential to cause commercial disruption . . . . Moreover, the disruptive effects of the . . . Act could be duplicated by other states seeking simultaneously to assert jurisdiction over a tender offer.

VI. WISCONSIN STATUTE SECTION 552: A STATE OF FLUX

In response to the constitutional attacks on state takeovers laws, a number of states, including Wisconsin, have amended their statutes in an attempt to avoid judicial invalidity. According to Richard Malmgren, the Wisconsin Commissioner of Securities and the author of the Wisconsin amendments, the

167. Id. at 90,033.
168. Id.
new Wisconsin takeover provisions are flexible enough to avoid the fate of those state statutes which have been invalidated.\textsuperscript{177} The amendments remove many of the problems which courts previously identified to invalidate state takeover laws. While the validity of the changes are unclear until challenged, they appear to provide for regulations which are compatible with the Williams Act.

The obstacles to an unfriendly tender offer are much less severe under the new provisions.\textsuperscript{172} Eliminated is the requirement that the commissioner of securities must, upon request by the target management, hold a hearing concerning a takeover registration. Instead, it is within the sole discretion of the commissioner.\textsuperscript{173} Also eliminated was one of the bases for denying registration. A finding that the tender offer is inequitable can no longer serve as a basis for denying registration.\textsuperscript{174} The denial of registration is only permitted where the corporate takeover law is violated, or the offeror is delinquent in filing ownership information, or where the offeror has included false or misleading information in the filing.\textsuperscript{175}

In addition, the amendment conforms all of the time requirements to the federal provisions.\textsuperscript{176} A comity provision is intended to avoid more than one state regulating a takeover.\textsuperscript{177} While this provision attempts to eliminate the major commerce clause objection to state takeover statutes, it appears to be flawed. The new section provides that the Wisconsin statute will not apply to any takeover regulated by another state. However, once the Wisconsin administrative decision is made, a target company could simply invoke the laws of a state without a similar provision.

Finally, the new law gives the commissioner a number of options in passing on a request for registration of a takeover. Previously, the commissioner could only approve or deny such

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171. Milwaukee Sentinel, June 29, 1981, sec. 2 at 7, col. 3.
172. Under prior law, friendly takeovers were excluded from takeover registration requirements. This new statute eliminates this exclusion. 1981 Wis. Laws ch. 16, § 9.
173. Id., § 9(4).
174. Id. at (5).
175. Id.
176. Id. at § 12.
177. Wis. Stat. § 552.05 (1979-1980).
\end{flushright}
a request.\textsuperscript{178} Now, the commissioner may also either postpone registration for up to 180 days or permit registration of an amended offer.\textsuperscript{179} In addition, the commissioner is also permitted to issue an exemption from registration, permitting a takeover offer to commence where the offeror’s purchase of securities is contingent upon subsequent registration.\textsuperscript{180} It is this final provision which will probably allow the Wisconsin statute to survive. It is now possible for the commissioner to review a tender offer without delaying in any way the commencement of the offer. Thus, the Wisconsin statute directly responds to the criticism which had previously been used to strike down state takeover laws. In addition, the elimination of fairness as a basis for denying registration places the Wisconsin statute outside the judicial criticisms of statutes.

\textbf{VII. Conclusion}

The administrative rules promulgated by the SEC make clear that state takeover laws are preempted by the Williams Act. The “market approach” taken by the federal law leaves no room for a fiduciary or “benevolent bureaucracy” approach. This is unfortunate due to the legitimate local interests present in state regulation.

Specifically, state approaches which are limited in jurisdictional reach to the target’s state of incorporation will probably survive commerce clause objections. Additionally, while precommencement or minimum period statutory provisions clearly conflict with the federal law, those statutes which have provisions for administrative review should be validated. First, the regulation of securities has traditionally been one where both the state and federal governments regulations are supplementary. Second, the market approach as envisioned by Congress restricts competition, and may not result in the best possible price the market will bear for the stock. In this way, the operative effect of the Williams Act results in a distinct advantage to the raiding company. If it is full disclosure and free flow of information that is sought, an opportunity to hear competitors should be afforded to target shareholders. How-

\begin{footnotesize}
\begin{enumerate}
\item[178.] 1981 Wis. Laws, ch. 16 § 9(5).
\item[179.] Id.
\item[180.] Id.
\end{enumerate}
\end{footnotesize}
ever, this can only be accomplished through Congressional action, given the position of the SEC with regard to preemption, coupled with the constraints of the judiciary in reviewing legislative purpose. While the Wisconsin approach probably avoids constitutional infirmity it is also a less useful tool for a target corporation to use in avoiding a takeover. Perhaps, with Congressional intervention, a legitimate state interest in protecting target corporations will be recognized.

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