Successful takeovers:
• target stockholders gain 20-35% or more

Unsuccessful takeovers:
• target stockholders gain little if not eventually taken over

Question: Why would target management resist a premium offer?
• Is entrenchment the only answer?

Types of Takeover Defenses

(1) Charter amendments

• must be approved by stockholders

• supermajority: 67% or more of votes necessary to approve control change
  • can be avoided by board ("board out")

• fair-price: supermajority clause can be avoided if price is high enough (P/E or P/B)
### Types of Takeover Defenses

#### (1) Charter amendments

- **staggered board:** Senate vs. House
  - only 1/K of board is elected each year, so it takes K years to turnover board completely

- **poison pills:** something to kill sharks that are eager to eat
  - rights to buy cheap shares if a control event occurs (only hostile deals)

#### (2) Legal/Regulatory/Antitrust Defenses

- **state corporation/anti-takeover laws** impose rules that are similar to stringent charter amendments for all corporations chartered in that state

  - changing state of incorporation can improve defense
(2) Legal/Regulatory/Antitrust Defenses

- If some activities of target (or bidder) firm are regulated, that may slow down successful bid
  
  - CBS used FCC regulation of broadcast licenses to ward off Ted Turner

(2) Legal/Regulatory/Antitrust Defenses

- Antitrust investigation can slow down bid
  
  - Cases frequently start from someone in the industry (e.g., the target)

  - Security Trust tried to ward off Norstar by buying some branches near Albany

  - Norstar promised to divest those branches if the takeover succeeded
Types of Takeover Defenses

(2) Legal/Regulatory/Antitrust Defenses

• Mobil's bid for Conoco failed, even though it had the highest nominal price
  • ignored by the market because the probability of a successful takeover was small for Antitrust reasons

• Interfirm litigation can be effective
  • e.g., target charges that bidder failed to disclose something material in SEC filings

• Ask a judge to enjoin bidder
  • stall tactic
  • Kaufman's bought McCurdy's, and was challenged by BonTon
<table>
<thead>
<tr>
<th>Types of Takeover Defenses</th>
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<tbody>
<tr>
<td><strong>(3) Asset Restructuring</strong></td>
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</table>
| • "Crown Jewel" defense: contract to sell attractive assets to a third bidder contingent on hostile bid  
  • e.g., Revlon |
| • "Pac Man" defense: make competing tender offer for shares of bidder  
  • Bendix/Martin Marietta (eventually acquired by United Tech) |

<table>
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<tbody>
<tr>
<td><strong>(4) Leveraged Recapitalizations</strong></td>
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</table>
| • partial LBO leaving equity holders with much riskier claims  
  • Phillips Petroleum after Pickens/Mesa bid, followed by Icahn interest  
  • generally increase stock value |
| **(5) ESOPs** |
| • employees get equity claim in the firm, but management votes the shares of the stock in the ESOP  
  • Polaroid after Shamrock attack |
### Types of Takeover Defenses

#### (6) Golden Parachutes

- Lump sum payments to target management if fired due to takeover
  - Usually small relative to size of deal, so probably not much deterrence effect
- Aligns the interests of target management with shareholders
  - But you don't want them taking just any bid

#### (7) "Greenmail" (targeted share repurchases, usually at a premium)

- Often linked with "standstill agreements" -- bidder will go away
- Bradley & Wakeman find that share repurchases ending takeover attempts have negative announcement returns
  - Reducing the probability of a control premium is bad news
- Should greenmail be outlawed?
## Types of Takeover Defenses: Summary

<table>
<thead>
<tr>
<th>Type of Defense</th>
<th>Description</th>
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<tbody>
<tr>
<td>Defenses where stockholders get to approve do not have large negative effects</td>
<td>- Management may not try anything too aggressive if shareholders have veto power</td>
</tr>
<tr>
<td>Defenses where target management has sole discretion have larger negative effects</td>
<td>- &quot;Crown Jewel&quot;, early pills</td>
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## Uses of Takeover Defenses

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<td>Target management has to try to get a higher bid from bidder</td>
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<td>- Like buying cars or appliances -- negotiation is assumed to be important</td>
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<tr>
<td>- If target saw a good bid and took it without resisting at all they are likely to be sued by stockholders because they should have gotten an even better deal</td>
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</table>
## Uses of Takeover Defenses

**Benefits from using defenses are:**

- (1) stall for more time to find a "White Knight"
- (2) directly compete with bidder (LBO, leveraged recap, Pac Man)
- (3) threaten high transaction costs (litigation, etc.) as part of bargaining strategy

## Uses of Takeover Defenses

**Costs of using defenses are:**

- (1) transaction costs (lawyers, investment bankers, etc.)
- (2) may deter some deals that would have been profitable with weaker defenses, but aren't now
  - entrenchment is easier
  - hard (impossible) to measure deals that never get tried
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