Takeovers, Poison Pills and Protectionism in Comparative Corporate Governance

Jennifer G. Hill
University of Sydney - Faculty of Law; Vanderbilt Law School; European Corporate Governance Institute (ECGI)
Takeovers, Poison Pills and Protectionism in Comparative Corporate Governance

Jennifer G. Hill
University of Sydney, Vanderbilt Law School and ECGI

© Jennifer G. Hill 2010. All rights reserved. Short sections of text, not to exceed two paragraphs, may be quoted without explicit permission provided that full credit, including © notice, is given to the source.

This paper can be downloaded without charge from: http://ssrn.com/abstract=1704745.

www.ecgi.org/wp
Takeovers, Poison Pills and Protectionism in Comparative Corporate Governance

November 2010

Jennifer G. Hill
Abstract

The regulation of hostile takeovers constitutes an interesting corporate governance microcosm. It is an area where clear contrasts in approach, regarding the balance of power between shareholders and the board of directors, are evident across different jurisdictions. Takeovers also reflect the dynamic operation of legal regulation (which includes the strategic responses of regulated parties themselves), and the growing tension between globalization and protectionism.

This paper analyses the regulation of hostile takeovers across a number of Western and Asian jurisdictions. First, the paper discusses the rise of takeovers and takeover defences in the United States. Against this backdrop, it examines recent developments in some other common law jurisdictions, such as the United Kingdom and Australia. It also raises the experience of the European Takeover Bid Directive, which Professor Hopt has described as “sobering”, in view of the large number of members states adopting a protectionist stance towards the directive’s implementation.

The theme of protectionism in takeovers is continued in discussion of takeovers and takeover defences in relation to two major Asian economies, Japan and China. As the paper shows, in spite of the apparent promise of open capital markets offered by globalization, protectionism is on the rise internationally and takeovers play a central role in this evolving story.

Keywords: hostile takeovers, takeover defences, poison pills, corporate governance, shareholders, directors, United States, United Kingdom, EU, Australia, Japan, China

JEL Classifications: G30, G 32, G34, G38, K22, K33

Jennifer G. Hill
University of Sydney - Faculty of Law
Faculty of Law Building, F10
The University of Sydney
Sydney, NSW 2006
Australia
phone: +61 2 9351 0280, fax: +61 2 9351 0200
e-mail: jennifer.hill@sydney.edu.au
Takeovers, Poison Pills and Protectionism in Comparative Corporate Governance

Jennifer G. Hill*

1. Introduction

“Forgive me, then, for bringing owls to Athens as a thanks-offering”.

Goethe

By the turn of the last decade, a range of factors had propelled comparative corporate governance to governmental and scholarly prominence. A range of factors had propelled comparative corporate governance to governmental and scholarly prominence. Fanned by globalisation and the influential “law matters” thesis, a central issue at that time became whether corporate governance regimes around the world would converge. Whereas some scholars considered this to be inevitable, others suggested that the very notion of “convergence” is ambiguous, and that the process is likely to be “slow, sporadic, and uncertain.”

This paper examines takeovers through a comparative law lens, and in the shadow of these fin de siècle debates. Takeover regulation constitutes an interesting corporate governance microcosm, where clear contrasts in approach are evident across jurisdictions. Context is crucial in this area, since takeover regulation confronts a range of principal-agent problems that may vary depending upon underlying corporate ownership structures. Takeovers also reflect the dynamic operation of legal regulation, which includes the strategic responses of regulated parties themselves. The structure of this paper is as follows. First, it discusses the rise of takeovers and takeover defences in the United States. Against the backdrop of the American experience, the paper then considers recent developments around the world, including in some other Western jurisdictions and two major Asian economies, Japan and China. As the paper shows, in spite of the apparent promise of open capital markets offered by globalisation and convergence theory, protectionism is on the rise internationally and takeovers play a central role in this evolving story.

2. Takeovers, Takeover Defences and the Balance of Power Between the Board and Shareholders in the US
2.1 The Rise of Takeovers in the US

“[O]ur corporate law is not static. It must grow and develop in response to, indeed in anticipation of, evolving concepts and needs”.

Unocal Corp v Mesa Petroleum Corp

The traditional mechanism in the United States for achieving corporate reconstructions was by way of merger, a procedure initiated and controlled by a company’s board, rather than its shareholders. Hostile takeovers made their first appearance in the US in the 1960s, and subsequently attained renown during the 1980s, aided by a smorgasbord of novel financing techniques, such as junk bonds. Takeovers offered the opportunity for potential acquirers to appeal directly to shareholders, thus bypassing the need to negotiate with the board.

The takeover boom of the 1980s revived corporate theory, which had languished since the early 20th century, raising fundamental questions about the nature and purpose of the corporation. Under agency theory, the market for corporate control emerged as the market’s “ultimate disciplinary tool.” Supporters of a free market for corporate control differed, nonetheless, on the role of directors in responding to an unsolicited bid. Some scholars suggested a limited power in target management to seek out competing bids; others advocated complete board passivity. The divergence reflects differing conceptions of “efficiency”. Professors Davies and Hopt have noted this tension, describing how rules that facilitate competing offers to enhance the bid price in particular transactions can, by deterring future initiating offers, effectively chill overall systemic efficiency of the market for corporate control.

Not everyone was equally sanguine about the corporate governance benefits of the market for corporate control. Takeovers, particularly of the bust-up variety, exposed stark conflicts of interest between various stakeholders in the corporate enterprise. Some influential managerialist commentators argued that the hostile takeover trend encouraged short-termism, predatory conduct by professional investors, harmed stakeholders and the community, and constituted a fundamental attack on the central role of the board under US corporate law. This critique provided an ideological justification for broad managerial discretion and paternalism toward shareholders, permitting the directors to fight fire with fire.

Unocal Corp. v Mesa Petroleum Corp. constituted a watershed decision in terms of consideration of agency conflicts, and the allocation of power between parties, in the takeover context. Recognising a target board’s “omnipresent specter” of self-interest, the Delaware Supreme Court assessed board conduct
by reference to an enhanced scrutiny test, requiring the board’s response to be “proportionate” to the threat posed by the hostile bid to the corporate enterprise. Yet the level of scrutiny under the Unocal test was malleable, and directors enjoyed considerable leeway in the exercise of their discretion, including the right to consider the interests of non-shareholder constituencies.29 Revlon, Inc. v MacAndrews & Forbes Holdings, Inc.30 subsequently constrained managerial power where a target company was up for sale, holding that in these circumstances stockholder interests would be paramount and obliging directors to attain the highest share price.31 Yet, in spite of Revlon32 and some early Delaware Chancery Court case law that gave real bite to Unocal’s proportionality test for assessing target board conduct,33 later Supreme Court decisions firmly reinstated a presumption of managerial fiat, in the absence of board action that was preclusive, coercive, or had the primary purpose of interfering with the shareholder franchise.34 Such approach is premised on the image of the board as less a gatekeeper than prime guardian of shareholder interests.35 This protector role for the board has been viewed as a vital antidote to the danger of coercive bids and as necessary to stimulate auctions to increase share price.36

2.2 The Poison Pill (and Other Managerial Barricades) and the Current Shareholder Empowerment Debate

"The takeover wars are over. Management won.”
Grundfest

These legal developments legitimised defensive conduct by US target boards from a theoretical perspective. All that was needed as a practical matter was an impregnable commercial strategy to impede unwelcome bids. This emerged with the 1982 creation of the celebrated poison pill, or shareholder rights plan.39 Poison pills involve the issuance of a new class of preferred stock to common shareholders of a potential target company prior to an acquisition.40 The stock contains inchoate rights, which will only be triggered by the acquisition of a specified percentage of target's stock.41 The rights typically entitle the target company's shareholders, but not the hostile bidder, to acquire additional common stock at a discounted price. The essence of the poison pill has been described as “discriminatory dilution” that makes a takeover bid more expensive and less palatable to a prospective acquirer. A significant part of the poison pill’s allure was that it could be adopted by the board without the need for shareholder approval.
US courts have typically been kind to poison pills. Within two years of their implementation, the Delaware Supreme Court declared poison pills valid; only in relatively rare cases have they been judicially rejected. \(^{45}\) City Capital Assocs. v Interco, Inc. \(^{46}\) represents an atypical case in which Chancellor Allen identified troubling aspects of poison pills from an accountability perspective, stating that in certain circumstances they threatened “to diminish the legitimacy and authority of our corporation law.” \(^{47}\)

Some US commentators have suggested that the potency of this form of takeover defence has been overstated. \(^{48}\) Nonetheless, when combined with a staggered board, the poison pill is indeed a formidable barrier to hostile bids. \(^{49}\) Under Delaware law, directors may be elected for a staggered term of up to three years, and, unless the certificate of incorporation provides otherwise, these directors can only be removed “for cause.”\(^{51}\) Such a limitation effectively insulates the directors by preventing an acquirer from obtaining control of the board in a single election.

By the early 1990s, a confluence of factors, such as the rise of constituency statutes, proliferation of poison pills, and less hospitable financial market conditions for takeovers,\(^{52}\) led one commentator to declare that the takeover wars were over, with management the clear victor. \(^{53}\) Nonetheless, this assessment was perhaps premature. These battles may simply have shifted to a new corporate governance arena: the current US shareholder empowerment debate. \(^{54}\) A broad-based law reform agenda is now underway to grant shareholders stronger rights vis-à-vis management in a range of contexts, including nomination of directors \(^{55}\) and executive remuneration decisions. \(^{56}\) These reform proposals have provoked fierce controversy and backlash in the United States. \(^{57}\) Also, in recent times there has been a sharp decline in staggered boards \(^{58}\) and poison pills \(^{59}\) at US companies due to institutional investor pressure.

3. A Comparison Between Takeover Law in the United States and Some Other Western Jurisdictions

“While the focus in the UK has been on attracting capital, the focus in the US has been on attracting managers”.

Rickford\(^{60}\)

“The experience with the implementation of the 13\(^{th}\) Directive on Takeovers is sobering indeed”.

Hopt\(^{61}\)
An apparent assumption of the “law matters” hypothesis was that there exists a standardised common law model of corporate governance, offering superior legal protections to those found in civil law jurisdictions. In fact, however, takeover laws in the United States and other common law jurisdictions, such as the United Kingdom and Australia, have divergent origins and have followed different paths in allocating power between shareholders and directors in takeovers.

Takeovers emerged earlier in the United Kingdom than the US, and appear to have been generally welcomed there as a panacea to the country’s post-WWII economic malaise. A number of scholars have noted, and sought to explain, the United Kingdom’s clear preference for shareholder interests in the takeover context, in comparison with the US pattern of deference to management. One possible explanation relates to regulatory structure. Some scholars have suggested that the UK self-regulatory regime, under the City Code on Takeovers and Mergers (“City Code”), has favoured institutional investors, unlike the US judicial model which supported managerial interests. There has also been a far lower level of tactical litigation in the United Kingdom than in the United States.

The contours of UK takeover regulation have been modified in recent times in accordance with European developments discussed below.

Australian takeover law provides an interesting contrast to these jurisdictions. The Australian regime, which has been described as “unique”, has several home-grown features that have tended to privilege equality of opportunity and fairness for minority shareholders over economic efficiency. The regime is particularly restrictive by international standards. Like many other jurisdictions, but unlike the US, Australian takeover law ensures that majority and minority shareholders share equally any control premium. However, whereas UK law permits private control transactions that pass the relevant takeover threshold provided a general offer or “mandatory bid” is then made to all shareholders, Australian takeover law prohibits an acquirer from passing the threshold except by means of a general bid.

Takeover disputes in Australia were, as in the United States, traditionally decided by the courts. However, this changed in 2000, when, in an attempt to reduce widespread tactical litigation, resolution of takeover disputes shifted to the Australian Takeovers Panel. This procedural shift also resulted in a doctrinal change in the assessment of defensive conduct by target boards. The Takeovers Panel departed from the courts’ previous fiduciary duty analysis of directors’ defensive conduct, substituting its own “frustrating action” policy, which focused on the effect, rather than the purpose, of the directors’ actions. This constituted a major shift in the balance of power between
the board of directors and shareholders during a bid under Australian law.\textsuperscript{81} The board is further constrained in both Australia and the United Kingdom by the fact that neither US-style poison pills,\textsuperscript{82} nor US-style staggered boards\textsuperscript{83} are legally permissible. Another common jurisdiction, Canada, permits poison pills,\textsuperscript{84} but they have evolved in an idiosyncratic way, to confer paramount control on shareholders.\textsuperscript{85}

What of Europe? Much ink has been spilled in recent years analysing the 13\textsuperscript{th} Directive on Takeovers, ("Takeover Bid Directive"),\textsuperscript{86} and the Byzantine route to its introduction,\textsuperscript{87} so discussion here will be limited to a few salient points. The directive’s apparent goals were to stimulate takeover activity in Europe and to create a level playing field through harmonisation.\textsuperscript{88} Key elements of the directive – the mandatory bid rule in Article 5 and the anti-frustration rule in Article 9 – were based on the London City Code.\textsuperscript{89} The controversial breakthrough rule in Article 11, which sought to achieve proportionality between capital and control, derived from recommendations of the 2002 Report of the High Level Group of Company Law Experts.\textsuperscript{90}

Ultimately, the Takeover Bid Directive may exemplify the potential gap in regulatory reform between motivation and outcome.\textsuperscript{91} According to one commentator, if the main goal of the directive was maximisation of takeovers, then it has been "a spectacular failure".\textsuperscript{92} Harmonisation\textsuperscript{93} was weakened by a political compromise that rendered the anti-frustration and breakthrough rules merely optional under Article 12.\textsuperscript{94} The majority of member states, perhaps unsurprisingly, have elected to opt out of these rules\textsuperscript{95} and some, such as France, have strengthened their anti-takeover defences.\textsuperscript{96} Also, in 2007 the proposed “one share, one vote” rule was abandoned in what has been called “a rare policy capitulation”\textsuperscript{97} by the European Commission.

In a recent paper, Professor Hopt describes the experience with the Takeover Bid Directive as “sobering,” in view of the large number of member states that appear to have adopted a protectionist stance towards the directive’s implementation in response to populist fears of globalisation.\textsuperscript{98} As the discussion below illustrates, this theme of economic protectionism is also of growing importance in parts of Asia.

4. Takeovers, Defensive Mechanisms and Protectionism: Recent Developments in Asia

4.1 Japan
“Until recently, Japan seemed destined to become the Galapagos Islands of the financial world.”

Nakamoto

Japan constitutes a fascinating and evolving case study in the takeover realm. In contrast to the United States, hostile acquisitions were until recently non-existent in Japan, due to the insulation provided by Japan’s elaborate system of cross-shareholding and keiretsu relationships. However, from the 1990s onwards, Japan’s capital market structure altered significantly as a result of corporate law reforms to enhance flexibility, the unravelling of stable cross-shareholdings, and increased foreign ownership. These changes provided a basis for hostile takeovers and increased attention to shareholder interests.

The effect of these corporate governance developments was revealed starkly in 2005, when Livedoor, an upstart Japanese internet company, launched a hostile takeover bid for Nippon Broadcasting, transforming the “unthinkable” into reality. In resultant litigation, the Tokyo District Court granted injunctive relief against a planned defensive stock warrant issue by the target board, on the basis that the directors’ conduct was designed to maintain current managerial and ownership control, and was “grossly unfair” under the Japanese Commercial Code. This decision was subsequently affirmed by the Tokyo High Court.

The Nippon Broadcasting litigation raised business community concern about the prospect of hostile takeovers, particularly by predatory foreign corporations. A flurry of government reports and guidelines concerning takeover defences followed. These included joint guidelines issued by the Ministry of Economy, Trade and Industry (“METI”) and the Ministry of Justice (“Guidelines”), which sanctioned the adoption of pre-bid defences in certain circumstances. Although the ostensible purpose of these non-binding Guidelines was to prevent “excessive defensive takeover measures”, in fact they provided Japanese companies with a blueprint for ensuring the validity of any defensive mechanisms. According to principles embedded in the Guidelines, takeover defences should seek to enhance corporate values and shareholder interests, reflect the shareholders’ will, and be “necessary and reasonable in relation to the threat posed”. Whereas the emphasis on shareholders’ will reflects a central principle under, for example, the UK and Australian takeover regimes, the final requirement is pure Delaware law. The Guidelines expressly contemplated discrimination against a hostile bidder, an important feature of poison pills. International business groups in Japan expressed anxiety that METI’s guidelines could obstruct, rather than improve, corporate governance and chill foreign investment.
As poison pills have declined in the United States, they have increased dramatically in Japan. The number of Japanese companies using this defence rose from two in 2004 to 340 in 2007, and 634 by 2008. The efficacy of poison pills as a defence mechanism in Japan was demonstrated in 2007, when a plan by the activist US hedge fund, Steel Partners LLC (“Steel Partners”), which held a 10% interest in the Japanese company, Bull-Dog Sauce Co (“Bull-Dog”), to acquire the remaining shares, foundered when Bull-Dog’s board adopted a poison pill that was subsequently approved by the target company’s shareholders. The pill was a standard dilution scheme, but with a condition that the potential acquirer would receive cash in lieu of the shares to which other shareholders were entitled. Steel Partners was unsuccessful in legal proceedings challenging the target board’s conduct. The Tokyo District Court, High Court and Supreme Court all ruled that the defensive measure was lawful, though on somewhat different lines of reasoning. The fact that the target shareholders had approved the defensive plan was a particularly significant factor in the District Court and Supreme Court judgments, and it is open to doubt whether a similar defensive plan would be sanctioned if enacted solely by management.

The Japanese Foreign Exchange and Foreign Trade Act of 1949 provides additional constraints by requiring advance notification and government approval for foreign investment in sectors deemed to be sensitive, such as national security. In September 2007, Japan widened the scope of industries subject to such notification and government review. The following year, METI raised national security objections to block an attempt by the UK hedge fund, The Children’s Investment Fund, to double its stake to 20% in J-Power (Electric Power Development Co), a Japanese electricity company with nuclear power aspirations. The acquisition by the Australian investment bank, Macquarie Bank, of a 20% stake in the Japanese company that owns Tokyo’s Haneda airport facilities also prompted intense political debate.

In spite of the resonance of US principles in recent corporate governance developments in Japan, few commentators consider this to provide evidence of any direct convergence toward a globalised standard. For example, although accepting Delaware takeover law principles, Japan appear more cautious about the related concept of the independent director. Institutional setting matters, and it appears that Japan may have adapted certain Western corporate governance principles, without displacing, and perhaps even strengthening, its traditional concept of the community firm. There have been some rare examples of successful shareholder activism, such as Steel Partners’ 2009 victory in replacing the board of Aderans, and recent evidence of a more shareholder-friendly stance by METI to encourage greater foreign investment. Nonetheless, Japan’s messages in this regard have been decidedly mixed. Poison pills have arguably proven to be a functional equivalent of Japan’s traditionally closed model of corporate governance, and protective cross-shareholdings are
reappearing. These developments have led the European Union Trade Commissioner to describe Japan, which has far less foreign investment than other developed economies, as “a globalisation paradox”. Others have simply declared that “Fortress Japan is back”.

4.2 China

“China is not and has never been a law-oriented culture”.

Tay

There is much current interest in corporate law developments in China. China is in the midst of “gaizhi,” or “transformation of the system”. This development has converted China from a state-controlled system to one with a mixture of state and private enterprise elements. China’s state-owned enterprises (“SOEs”) have been gradually transformed into partially privatised organisations, often in tranches. This mode of restructuring has enabled the Chinese government to maintain strategic levels of control in certain enterprises.

Like Japan, China was formerly insulated from the market for corporate control, but within the space of only a decade, M&A transactions are now a recognised feature of the corporate landscape. These economic developments have generated a torrent of corporate legislation in a country which historically relied upon administrative regulations and neibu, rather than law. The market regulator, the China Securities Regulatory Commission (“CSRC”) introduced new takeover regulations in 2002 and 2006, with further amendments in 2008.

China's emerging takeover law is interesting from the dual perspectives of the "law on the books" issue and protectionism. China’s "on the books" takeover law is state of the art, containing, for example, a mandatory bid requirement of a 30% acquisition threshold to ensure sharing of a control premium and fairness between majority and minority shareholders. However, to date, there has been a wide gap between China's formal takeover law and its operation in practice. The CSRC possesses a broad discretion to waive the 30% mandatory bid rule on a case-by-case basis. The CSRC has exercised this waiver power so often as effectively to subvert the operation of the mandatory bid rule altogether. It also appears that the rule may not apply to acquisitions of control involving government-mandated transfers or allocation of State-owned assets.
Trade protectionism is on the rise in China through a variety of different legal techniques. Waivers of the mandatory bid rule could potentially be used in this way to discriminate between domestic and foreign bidders. Waivers could constitute a subtle, and low visibility, way in which certain market players could receive favourable treatment within a protectionist framework.

In the wake of the global financial crisis, China has been on both sides of several recent international M&A skirmishes with protectionist overtones. In March 2009, the Chinese Ministry of Commerce (“Mofcom”) used new competition laws, introduced as a condition to China’s accession to the WTO, to block a $2.4 billion bid by Coca-Cola Co for China Huiyuan Juice Group Ltd (“Huiyuan Juice”), in what would have been the largest foreign takeover of a Chinese company. The Huiyuan Juice takeover bid was seen as a litmus test in determining China’s willingness to give foreign companies greater latitude in acquiring Chinese companies. Although Chinese officials publicly denied trade protectionism in relation to the proposed deal, critics have argued that the Mofcom decision perpetuates foreign investment obstacles, particularly where loss of leading Chinese brands is at issue.

China’s investments abroad have grown exponentially in recent years, rising from $143 million in 2002 to $40.7 billion in 2008. Increasingly, however, Chinese companies seeking such investment opportunities have themselves experienced protectionist pressures. A high profile example of this phenomenon occurred when the Chinese oil production company CNOOC Ltd withdrew an $18.5 billion bid for Unocal Corp in 2005, in the face of intense pressure from the US Congress.

More recently, Chinese corporations, seeking to buy stakes in the Australian resource sector, have received variable responses from Canberra. Under Australian law, the Federal Treasurer is the ultimate arbiter of foreign investment decisions, advised by the Foreign Investment Review Board (FIRB). In March 2009, only one week after the Chinese government rejected Coca-Cola’s bid for Huiyuan Juice, the Australian government blocked a $1.8 billion bid by China Minmetals Nonferrous Metals Co. for the Australian company Oz Minerals Ltd, on “national security” grounds. However, in the same month, Canberra approved an acquisition by Hunan Valin Iron and Steel of up to 17.55% of Fortescue Metals, Australia’s third largest iron ore exporter.

The most controversial transaction in Australia to date is the attempted acquisition by Chinalco of a $19.5 billion stake in the Anglo-Australian mining group Rio Tinto (“Rio”) in 2009. This constituted the largest overseas investment ever announced by a Chinese company. The proposal included terms that would have entitled Chinalco to a boardroom presence at Rio as well as joint venture marketing rights in
relation to the iron ore. Critics of the proposed transaction relied on the Chinese government’s veto of Coca-Cola’s bid for Huiyuan Juice as justification for an analogous rejection by the Australian government of Chinalco’s bid. The government was, however, spared the need to rule on the acquisition, since the planned deal ultimately collapsed in acrimonious circumstances. Rio, faced with shareholder opposition, abandoned Chinalco’s proposal in favour of a joint venture with its Anglo-Australian competitor BHP Billiton Ltd (“BHP”). Speculation continues as to the possibility that the Chinese government might attempt to use its anti-monopoly powers, which have extra-territorial force, to challenge the Rio-BHP joint venture.

Scholars have predicted that, in spite of China’s adoption of many Western style reforms, it remains highly unlikely that legal convergence will occur. Rather, as in the case of Japan, it seems probable that China will adapt these reforms and ultimately retain its own distinctive legal tradition.

5. Conclusion

“Convergence in one area will be paralleled by renewed divergence in another.”

Hirshman

Fundamental differences exist in takeover regimes, not only between common law and civil law jurisdictions, but also within the common law world itself. The allocation of power between corporate controllers and shareholders will vary, depending upon underlying corporate theory and who is viewed as the greater threat – a hostile bidder or the target company’s own management. The paper discusses developments concerning takeovers and takeover defences in a number of jurisdictions, including some, such as Japan and China, which have not until recently had a market for corporate control.

Some scholars have considered convergence of takeover law to be inevitable. The developments discussed in this paper undoubtedly exhibit some common themes, such as the rise of protectionism in takeover law. However, they also show the dynamic nature of legal regulation, including adaptive conduct by regulated parties, and the uncertainty of outcome in legal transplantation, given underlying differences in legal cultures and enforcement mechanisms. These developments serve as a reminder that a gap that often exists between motivation and outcome in regulatory reform, and that convergence is indeed an uncertain process.
Letter from Goethe to Wilhelm von Humboldt, (Sept. 1, 1816), available at http://www.gutenberg.org/files/11366/11366-8.txt. Speaking on the subject of takeovers to an English audience in 2002, Professor Hopt said that he felt as if he were "carrying owls to Athens", or in the English vernacular, "carrying coals to Newcastle" (Klaus J. Hopt, Takeovers, Secrecy, and Conflicts of Interest: Problems for Boards and Banks, in TAKEOVERS IN ENGLISH AND GERMAN LAW 33, 33 (Jennifer Payne, ed., Hart Publishing, 2002)). I share this sentiment in writing on the same topic, given Professor Hopt’s expertise in this area.


The “law matters” hypothesis postulated that capital market structure was directly linked to a country’s corporate governance regime. See, e.g., Rafael La Porta, Florencio Lopez-de-Silanes & Andrei Shleifer, Corporate Ownership Around the World, 54 J. FIN. 471 (1999); Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer & Robert Vishny, Law and Finance, 106 J. POL. ECON. 1113 (1998).


Curtis J. Milhaupt, Property Rights in Firms, in CONVERGENCE AND PERSISTENCE IN CORPORATE GOVERNANCE 210, 213 (Gordon & Roe eds., Cambridge Univ. Press 2004).

See generally Klaus J. Hopt, Obstacles to Corporate Restructuring: Observations from a European and German Perspective, in PERSPECTIVES IN COMPANY LAW AND FINANCIAL REGULATION 373, 376 (Michel Tison et al. eds., Cambridge Univ. Press, 2009).


Generally, a US statutory merger will be approved by the boards and shareholders of each constituent corporation. The board acts as gatekeeper in determining which transactions should be considered by shareholders. See CHARLES R.T. O’KELLEY & ROBERT B. THOMPSON, CORPORATIONS AND OTHER BUSINESS ASSOCIATIONS: CASES AND MATERIALS 621, 755 (5th ed. 2006).

See JESSE H. CHOPER, JOHN C. COFFEE & RONALD J. GILSON, CASES AND MATERIALS ON CORPORATIONS 945 (7th ed. 2008).


Id. at 229-230; John C. Coffee, Shareholders versus Managers: The Strain in the Corporate Web, 85 MICH L. REV. 1, 13 (1986).

See Martin Lipton, Takeover Abuses Mortgage the Future, WALL ST. J., April 5, 1985.

Martin Lipton, Takeover Bids in the Target’s Boardroom, 35 BUS. LAW. 101,105-106 (1979).

Id. at 113, 123.

493 A. 2d 946 (Del. 1985).


Unocal, 493 A.2d at 955.

506 A.2d 173 (Del. 1986).

See, e.g., City Capital Assoc. v. Interco, Inc, 551 A.2d 787, 798 (Del. Ch. 1988), where Chancellor Allen noted that the alleged “threat” was “far too mild” to justify the board’s decision to keep a poison pill in place.


A wide variety of defensive tactics were used in the early 1980s, including, for example, shark repellents, greenmail and white knights. Kahan & Rock, supra note 17, at 874.


For a detailed discussion of the technical operation of a shareholder rights plan, see Carney & Silverstein, supra note 39, at 183-186.


Kahan & Rock, supra note 17, at 909. For discussion of a battle between the shareholders and directors of News Corporation concerning this aspect of poison pills, see generally Jennifer G. Hill, Subverting Shareholder Rights: Lessons from News Corp’s Migration to Delaware, 63 VAND. L. REV. 1, 29ff (2010).


The Delaware courts have invalidated some variations of the shareholder rights plan, such as so-called “dead hand” and “no hand” poison pills. See, e.g., Carmody v. Toll Brothers, Inc., 723 A.2d 1180 (Del. 1998); Quickturn Design Systems, Inc v. Shapiro, 721 A.2d 1281 (Del. 1998).

551 A.2d 787 (Del. Ch. 1988).

City Capital Assoc. v. Interco, Inc, 551 A.2d 787, 799-800 (Del. Ch. 1988). Responding to the Interco case, Martin Lipton sent a memo to his clients depicting the decision as a “dagger aimed at the hearts of all Delaware corporations.” Memorandum from Wachtell, Lipton, Rosen & Katz to clients, You Can't Say No

Kahan & Rock, supra note 17, at 871; See Carney & Silverstein, supra note 39, at 182. Carney and Silverstein consider that “the typical poison pill will make many bidders nauseous, but that it will not be fatal in most cases.” Id. at 181. Cf. Geis, supra note 42, at 1201.


Kahan & Rock, supra note 17, at 878-879.

Grundfest, supra note 37, at 858.

Lipton, supra note 39, at 1369. See generally Jennifer G. Hill, The Rising Tension Between Shareholder and Director Power in the Common Law World, CORPORATE GOVERNANCE: AN INTERNATIONAL REVIEW (forthcoming 2010).


See, e.g., Lawrence Mitchell, Protect Industry from Predatory Speculators, FIN. TIMES, July 8, 2009, at 9; Martin Lipton, Jay Lorsch & Theodore Mirvis, Schumer’s Shareholder Bill Misses the Mark, WALL ST. J., May 12, 2009, at A15.


Klaus J. Hopt, Obstacles to Corporate Restructuring: Observations from a European and German Perspective, in PERSPECTIVES IN COMPANY LAW AND FINANCIAL REGULATION 373, 373 (Michel Tison et al. eds., Cambridge Univ. Press, 2009).


Takeovers developed from the 1950s in the United Kingdom. See Cheffins, supra note 63, at 360-361; Cranston, supra note 63, at 79.


Under the UK takeover regime, a specialised non-judicial body, the Panel on Takeovers and Mergers administers the City Code on Takeovers and Mergers.


See Ogowewo, supra note 42, at 607–09.

Id. at 590-92.


The 1969 Second Interim Report of the Company Law Advisory Committee (“Eggleston Committee Report”) has been described as the “conceptual grundnorm” of Australia’s takeover regime. Id. at 337.

Id. at 338.

For discussion of the benefits and potential costs to a mandatory bid rule, see Paul L. Davies, The Notion of Equality in European Takeover Regulation, in TAKEOVERS IN ENGLISH AND GERMAN LAW 9, 22-28 (Jennifer Payne, ed., Hart Publishing, 2002).

Mannolini, supra note 73, at 357-58.


The general consensus appears to be that the Australian Takeovers Panel has been a success. See generally McKeon & Farrer, supra note 78; Emma Armson, Models for Takeover Dispute Resolution: Australia and the UK, 5 J. CORP. L. STUD. 401 (2005).


For a detailed analysis of the reasons why U.S.-style poison pills are impermissible under Australian and UK law, see Jennifer G. Hill, supra note 80, at 134-38.

See Corporations Act, 2001 § 203D (Austl.); Companies Act, 2006 c. 46 § 168(1) (U.K.), which grant shareholders an absolute right to remove directors with or without cause.

See INST. S’HOLDER SERV., supra note 59, at 11-13.


Nilsen, supra note 87, at 1.


Complexity abounds, however, in the opt-in/opt-out interplay for member states and companies under Article 12. See Hopt, supra note 89, at 263.


France, for example, introduced a form of poison pill. See Wymeersch, supra note 93, at 7; INST. S’HOLDER SERV., supra note 59, at 6-7.

Andrew Bounds & Kate Burgess, EU Scraps Plan for "One Share, One Vote" Reform, FIN. TIMES, Oct. 4, 2007, at 1; Hopt, supra note 61, at 392.

Hopt, supra note 61, at 378-381. See also REPORT ON THE IMPLEMENTATION OF THE DIRECTIVE ON TAKEOVER BIDS, supra note 95, at 10. Professor Hopt notes, however, that another interpretation of the
directive’s implementation is one of path dependency, rather than protectionism. Hopt, supra note 61, at 380.


Davies & Hopt, supra note 22, at 273.

See Gilson & Roe, supra note 2, at 882.


The value of shares held in cross-shareholding arrangements in Japanese companies declined from 33% in 1991 to 11.1% in the fiscal year ending March 2006. See Andrew Morse & Sebastian Moffett, Japan’s Companies Gird for Attack – Fearing Takeovers, They Rebuild Walls; Rise of Poison Pills, WALL ST. J., Apr. 30, 2008 at A1. Foreign ownership of Japanese shares increased from 4.1% in 1987 to 27.6% in 2008. See Alison Tudor, Advocate Pitches Reform in Japan, WALL ST. J., Apr. 9, 2009, at C2.


For detailed background of this control contest, see generally Sadakazu Osaki, Regulation of Japan’s Capital Markets and the Battle for Control of Nippon Broadcasting System, 8 NOMURA CAPITAL MARKET REV. 25 (2005); Curtis Milhaupt & Katharina Pistor, The Livedoor Bid and Hostile Takeovers in Japan: Postwar Law and Capitalism at the Crossroads, in LAW AND CAPITALISM: WHAT CORPORATE CRISIS REVEAL ABOUT LEGAL SYSTEMS AND ECONOMIC DEVELOPMENT AROUND THE WORLD 87 (Univ. of Chicago Press, 2008).


Osaki, supra note 105, at 34-36.


See GUIDELINES, supra note 104.
These circumstances included situations where, for example, the defense was in response to a coercive bid, where defensive measures could benefit shareholders. *Id.* at 2-5. The Tokyo High Court decision in the Nippon Broadcasting litigation also provided examples of exploitative takeovers, where defensive tactics might be justified. *Id.* at 16; Osaki, *supra* note 105, at 25.

*GUIDELINES, supra* note 104, at 1.

*Id.* at 3-6.

See Milhaupt & Pistor, *supra* note 110.

*GUIDELINES, supra* note 104, at 7-8, 11-12.


INST. S’HOLDER SERV., *supra* note 59.


*Id.* at 345, 354-56.

In contrast, the Tokyo High Court focused on the bidder, categorising Steel Partners as an “abusive acquirer” due to its pattern of quickly selling off acquired corporations, thereby confirming the appropriateness of defensive methods. *Id.* at 354-55.


See e.g., Foreign Exchange and Foreign Trade Act, Law No. 228 of 1949, art. 26-27, 55-56.

See USGAO Report, *supra* note 119, at 75.

*Id.* at 12; Morse & Moffett, *supra* note 103, at A1.


Gilson, *supra* note 102.
Buchanan & Deakin, supra note 109, at 20-22.


See Tudor, supra note 103, at C2; Nakamoto, supra note 128.

In 2008, for example, Takao Kitabata, a Vice Minister of METI, described shareholders as “fickle, irresponsible and greedy”. See Michiyo Nakamoto, One-way Street? As Its Companies Expand Abroad, Japan Erects New Barriers at Home, FIN. TIMES, March 3, 2008, at 7.


See Nakamoto & Burgess, supra note 134; Morse & Moffett, supra note 103.

See USGAO Report, supra note 119, at 73. In 2006, foreign direct investment in Japan was 2.5% of gross domestic project, compared to 44.6% in the UK and 33.2% in France. See Michiyo Nakamoto, Struggle to Sweep Away Barriers to Change, FIN. TIMES, March 19, 2008 at 1.

Leo Lewis, Peter Mandelson Raps Japan’s Investment Hostility, TIMES ONLINE, April 22, 2008.

Morse & Moffett, supra note 103.


Id. See also Knowledge@Wharton, The Long and Winding Road to Privatization in China, May 10, 2006.

See generally Ross Garnaut et al., supra note 143, at xi-xiv; Stephen Green, TWO-THIRDS PRIVATISATION – HOW CHINA’S LISTED COMPANIES ARE – FINALLY – PRIVATISING (The Royal Inst. of Int’l Affairs, 2003).


Stanley Lubman, Looking for Law in China, 20 COLUM. J. ASIAN L. 1, 6-7 (2006).

Measures for Administration of the Acquisition of Listed Companies were promulgated by the CSRC on September 28, 2002 and became effective on December 1, 2002. See generally PAUL, WEISS, RIFKIND, WHARTON & GARRISON, MEASURES FOR ADMINISTRATION OF THE ACQUISITION OF LISTED COMPANIES 2-5 (2002) [hereinafter Measures].

Investment by Sovereign Wealth Funds and State Owned Enterprises: Are Our Rules Right?

For a discussion of Australia’s foreign investment regulatory regime, including proposed 2009 amendments to extend its reach, see Greg Golding & Rachael Bassil, Australian Regulation of Foreign Direct Investment by Sovereign Wealth Funds and State Owned Enterprises: Are Our Rules Right?, Address to the Law Council Corporations Law Committee, 2009 Corporate Law Workshop (Sept. 12, 2009).

Peter Smith, *Hunan Stake in Fortescue Approved*, FIN. TIMES, April 1, 2009, at 16.

For background on the deal, see generally Outmanoeuvred, supra note 162.


The state-controlled newspaper, the Beijing Times, was particularly critical of events, stating, "Poor Chinalco prepared the wedding clothes but when the peach was ripe somebody else plucked it." Outmanoeuvred, supra note 162.


See, e.g., Lubman, supra note 148, at 91-92; Erh-Soon Tay, supra note 142, at 159-161.


Hill, supra note 5, at 748.

See, e.g., Hansmann & Kraakman, supra note 6, 457-58.


Langevoort, supra note 91.

Milhaupt, supra note 8, at 213.
about ECGI

The European Corporate Governance Institute has been established to improve corporate governance through fostering independent scientific research and related activities.

The ECGI will produce and disseminate high quality research while remaining close to the concerns and interests of corporate, financial and public policy makers. It will draw on the expertise of scholars from numerous countries and bring together a critical mass of expertise and interest to bear on this important subject.

The views expressed in this working paper are those of the authors, not those of the ECGI or its members.

www.ecgi.org
ECGI Working Paper Series in Law

Editorial Board

Editor  
Eilis Ferran, Professor of Company and Securities Law, University of Cambridge Law Faculty and Centre for Corporate and Commercial Law (3CL) & ECGI

Consulting Editors  
Theodor Baums, Director of the Institute for Banking Law, Johann Wolfgang Goethe University, Frankfurt & ECGI  
Paul Davies, Allen & Overy Professor of Corporate Law, University of Oxford & ECGI  
Henry B Hansmann, Augustus E. Lines Professor of Law, Yale Law School & ECGI  
Klaus J. Hopt, Director, Max Planck Institute for Foreign Private and Private International Law & ECGI  
Roberta Romano, Oscar M. Ruebhausen Professor of Law and Director, Yale Law School Center for the Study of Corporate Law, Yale Law School & ECGI  
Eddy Wymeersch, Chairman, CESR & ECGI

Editorial Assistant :  
Paolo Casini, LICOS, Katholieke Universiteit Leuven  
Lidia Tsyganok, ECARES, Université Libre De Bruxelles

Financial assistance for the services of the editorial assistant of these series is provided by the European Commission through its RTN Programme on European Corporate Governance Training Network (Contract no. MRTN-CT-2004-504799).
Electronic Access to the Working Paper Series

The full set of ECGI working papers can be accessed through the Institute’s Web-site (www.ecgi.org/wp) or SSRN:

|----------------------|----------------------------------------|