A takeover law for New Zealand - an American perspective

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Christopher Hogg, who is an associate of a New York city law firm specialising in securities and corporate law, here considers the respective takeover regimes of New Zealand and the United States. He identifies some deficiencies in the former and discusses the aims and processes of the American system, concluding that some of its aspects may be suitable for adoption in New Zealand.

I. INTRODUCTION

New Zealand has never had an effective legislative scheme regulating takeovers. Only recently, in the wake of a veritable tidal wave of takeover activity, has the question of enacting such a takeover code arisen. In a largely unregulated environment, there is a concern that some rules are needed to prevent large and sophisticated market players from trampling those who are only just entering the takeover game. On the other hand, there is the fear that the introduction of rules may not be absolutely necessary and may even discourage takeovers. At the centre of the debate is the Securities Commission[1] which is now considering whether such a law should be enacted and if so, what form it should take.[2] This article's principal purpose is to consider some of the aims a New Zealand takeover law might seek to accomplish and to outline a possible method of achieving those aims which is suggested by takeover legislation in the United States.

The takeover phenomenon that New Zealand is now experiencing is reminiscent of the boom that began in the United States in the 1960s and which is still continuing, if not increasing in size. The American takeover explosion led to federal legislation in 1968, which is commonly known as the "Williams Act" after its sponsor, Senator Harrison Williams.[3] The Williams Act appears to have struck that delicate balance between shareholder protection and

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1 Referred to in this paper as the "Commission".

2 The Commission has prepared a three-volume review of takeover law, hereinafter referred to as the "Review". Chapter 7 of the Review includes a set of general legislative proposals in respect of which the Commission requested submissions.

3 15 U.S.C. §§ 78m(a), 78m(e), 78n(d)-(8), hereinafter referred to as the "Williams Act".

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excessive regulation. This is not to say that the American model is a perfect one — far from it — its complexity alone robs it of that accolade. The success of the legislation, however, suggests that it might be a useful comparative model for such a law in New Zealand.

Obvious differences in size and structure between the American capital markets and those of New Zealand militate against slavish imitation of the Williams Act. But there is much to be learned from the philosophy and structure of the United States legislation. Guided by the concept of disclosure, the Williams Act effects only minimal interferences with the structure of takeover bids but mandates the dissemination of full and adequate information to all shareholders to whom the bid is directed. This article will postulate a New Zealand takeover law based on a similar philosophy — interfering with takeovers only so far as to ensure that target shareholders receive adequate information and adequate time to consider it.

In an effort to identify some of the aims a New Zealand takeover law might seek to accomplish, the first part of this article will consider the various sources of existing New Zealand law that impact on takeovers and will suggest areas in which legislation might be helpful.

Part two of the article will focus on the Williams Act. First, it will discuss the origins and aims of that legislation, and secondly, it will outline the legislation itself. A complete description of American takeover law is not the aim of this section. Rather, it is intended to describe the structure and principal features of the law in order to highlight those aspects which might be applicable in New Zealand.

In the conclusion of the article, a distillation of some of the more helpful features of the American legislation which might be useful in New Zealand will be attempted.

II. EXISTING NEW ZEALAND TAKEOVER LAW — THE NEED FOR CHANGE

A. *Overview*

New Zealand is without a comprehensive legislative scheme regulating takeovers. The various pieces of legislation that do exist have developed in a piecemeal fashion, each oriented towards a particular aspect of the takeover phenomenon. There are three principal statutes impacting to varying degrees upon takeovers in New Zealand:

- the Companies Act 1955 and, particularly, the Companies Amendment Act 1963, which ostensibly regulate all takeover activity, but which have largely been rendered obsolete by changing takeover tactics.
- Part III of the Commerce Act 1975, as recently amended, contains, inter alia, a pre-takeover review procedure, which is confined to monopoly and antitrust concerns.[4]
- the Overseas Investment Act 1973 and the regulations under that Act, whose main

4 The Commerce Act review procedure is similar to that in the United States Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a et seq.

object is the implementation of national policies relating to overseas investment in New Zealand.[5]

In addition to the statutes, there are two other sources of law:

— the rules of the New Zealand Stock Exchange which are, perhaps, the most effective regulatory scheme but which are without the force of statutory law.

— the Common Law of conspiracy, fraud, misrepresentation and fiduciary duty.[6]

B. *The Companies Amendment Act 1963 and the Companies Act 1955*

The principal legislation on takeovers in New Zealand is contained in Part I of the Companies Amendment Act 1963.[7] The 1963 amendment makes it unlawful to commence a "takeover offer", as defined, except by making the disclosure required by the legislation. The purpose of the 1963 amendment was described by the Minister of Justice in terms strikingly similar to the stated purpose of the American Williams Act.[8] In introducing the Bill the Hon. Mr. J. R. Hanan M.P. said:[9]

> The first provision of the Bill dealing with takeovers is designed to lay down a set of requirements to which those making takeover bids must conform. The Government does not want to discourage takeover bids — that is not the Government's business. It wishes simply to ensure that shareholders are given certain information about the offer made, and that they are also given a certain time in which they can study the terms and obtain expert advice. The company whose shares are to be acquired must be advised in adequate time so that the directors can decide whether or not they should recommend the offer to shareholders.

Unfortunately, the 1963 amendment has a very limited application. First, two classes of transaction are expressly exempted under section 3.[10] Secondly, and more significantly, the Act only applies to written takeover offers.[11] Since the concept of a written offer has been very narrowly defined by the courts, an offeror has only to "stand in the market" and orally announce his bid to avoid the strictures of the 1963 Act.[12] Ironically, therefore, far from guaranteeing target shareholders the disclosure it requires, the 1963 amendment has the effect of encouraging bidders to make offers without any disclosure at all!

5 Since it relates only to the narrow field of foreign investment in New Zealand, the Overseas Investment Act 1973 is not discussed here.

6 Since Common Law remedies have little impact on takeovers and would, likely, not be affected by a takeover law, they are not discussed in detail here.

7 Companies Amendment Act 1963, hereinafter referred to as the "1963 amendment", ss. 2-14.

8 See infra, n.33.

9 N.Z. Parliamentary debates vol. 336, 1963: 2017.

10 The exempted transactions are: (i) the acquisition of shares in a private company where all the offerees have waived the requirements of the 1963 amendment s.3(a); and (ii) an offer as part of a "takeover scheme" to six or fewer shareholders, s.3(b). The second exemption also has the problem that the concept of a "takeover scheme" is so elusive as to be positively unhelpful. See the Commission's Review, vol. I, pp. 14-15.

11 See s.2 of the 1963 Act; *Multiplex* v. *Speer* [1966] N.Z.L.R. 122, 150; *Carter Holt Holdings Ltd.* v. *Fletcher Holdings Ltd.* [1980] 2 N.Z.L.R. 80, 86.

12 See *Tatra Industries Ltd.* v. *Scott Group Ltd.* (H.C. Wellington No. A 244/83, Judgment 19 August 1983). Notice of Intention to stand in the market under Stock Exchange Rules, not a "takeover offer".

The Companies Act 1955 contains four other groups of provisions relating to various aspects of takeover activity:[13]

— the regulation of payments to company directors, generally prohibiting payments to directors for loss of office, absent disclosure and stockholder approval.[14]

— prohibitions on a company financing the purchase of its own shares.[15]

— a procedure for the compulsory acquisition of an outstanding remainder of shares after a takeover offer.[16]

— a procedure for the amalgamation and reconstruction of companies.[17]

New Zealand's Companies Act, as amended, does not effectively regulate takeovers. First, the 1963 amendment is so limited in scope, both by its terms and by judicial interpretation, that it cannot effectively operate to achieve its intended goal — ensuring that target shareholders have sufficient time and information to consider the merits of the bid. Secondly, the general provisions scattered throughout the Companies Act which impact on takeovers also do not operate to guarantee shareholder disclosure, except in certain limited circumstances.

C. *Part III of the Commerce Act 1975*

Part III of the Commerce Act 1975, as amended, establishes a takeover review procedure which is confined to monopoly and antitrust considerations.[18] Under the Commerce Act, initial notification of a "takeover proposal" is made to the Chairman of the Commerce Commission.[19] The Chairman decides whether the proposal will be considered under the "fast track" method (where the proposal is referred to the Examiner of Commercial Practices for possible decision within twenty-five working days) or the "slow track" (where the proposal is investigated by the Examiner and decided by the Commission within as much as 100 working days).

The Commerce Act review procedure only applies to "takeover proposals" for the acquisition of 20 per cent or more of the target's stock.[20] Moreover, the Commerce Act does not mandate disclosure of the bid to either the target or its shareholders.[21] Thus, this legislation, even as amended, does not offer target shareholders any disclosure or timing guarantees.

D. *The Rules of the New Zealand Stock Exchange*

The rules of the New Zealand Stock Exchange contain perhaps the most effective regulatory scheme of takeovers in New Zealand. Section 6 of the rules contains a "takeover code" which requires:

13 Referred to in this paper as the "Companies Act". These provisions are extensively discussed by the Commission in its Review, vol. I, pp. 16-24.
14 Companies Act, ss. 191-194.
15 Ibid., s. 62.
16 Ibid., s. 208.
17 Ibid., ss. 205-207.
18 Part III of the Commerce Act 1975 was extensively amended by the Commerce Amendment Act 1983, which came into effect on 1 April 1984.
19 See ss. 68 and 73B of the Commerce Act.
20 See s.67 of the Commerce Act.
21 The Commission recommends requiring disclosure in its Review, vol. I, p. 27.

— disclosure of the terms of the bid to target shareholders.[22]
— giving target shareholders time to consider the bid.[23]
— general restrictions on insider trading.[24]
— general restrictions on defensive tactics.[25]
— proration for partial bids and increases in offering price.[26]

While the coverage of the takeover code is comprehensive, its language is general and precatory rather than specific and mandatory. Thus, while it is, doubtless, an effective guide to the honest, it does little to control the activities of the unscrupulous. Moreover, the Stock Exchange code operates only as a contract among listed companies and brokers.[27] Thus, sanctions for violation of the rules are confined to delisting of a company's securities or disciplining a broker.

Since the New Zealand Stock Exchange provides the only forum in which the securities of public companies may be traded, delisting may be a serious sanction — perhaps too serious for minor infringements of the code. Moreover, those who suffer most from the delisting of a company's shares are its shareholders who, likely, had nothing to do with the breach of the code but who would be denied the opportunity of selling their stock if it was delisted. Ironically, therefore, the penalties of the code may hurt those most who it seeks to protect — offeree shareholders.[27a] In addition, the code is powerless against an insurgent using a private company as a takeover vehicle.

E. *Conclusion*

New Zealand currently has no law capable of satisfying the purposes of both the 1963 amendment and the Stock Exchange rules — ensuring shareholders receive adequate time and information to consider the merits of a takeover bid.[28] The 1963 amendment itself does not meet this goal because it may so easily be circumvented. The Stock Exchange rules, the most effective existing set of regulations, are also not completely satisfactory because of their general language and lack of effective sanctions. The other pieces of existing legislation are confined to specific areas and do not pretend to establish any general scheme for the regulation of takeovers.

New Zealand is, thus, without any effective scheme for regulating takeovers. As a result, bids may be made in a hurried fashion without any accompanying disclosure at all. It is submitted that among the more significant problems caused by these tactics are the following:

22 Paragraphs 607 and 608.
23 Idem.
24 Paragraphs 602 and 603.
25 Paragraph 609.
26 Paragraph 613.
27 See *Stock Exchange Association of New Zealand* v. *Commerce Commission* [1980] 1 N.Z.L.R. 663; *N.Z. Forest Products Limited* v. *New Zealand Stock Exchange* (1984) 2 N.Z.C.L.C. 99, 051.
27a See *Norlin Corp.* v. *Rooney, Pace Inc.* [1984] Fed. Sec. L. Rep. (CCH) ¶ 91, 564 (2nd Cir., 27 June 1984) where the Second Circuit Court of Appeals regarded delisting as ipso facto causing injury to shareholders.
28 See speech of the Hon. Mr. J. R. Hanan M.P., supra n.9.

— where takeover bids are made in secret, through market purchases, target shareholders may be deprived of the opportunity to receive the premium share prices which are often associated with the sale of corporate control;
— where takeover bids are made in great haste and relative secrecy, small shareholders may not realise that a bid is being made or they may acquire knowledge or understanding of a bid too late to participate in the control premium;
— where takeover bids are made in great haste shareholders who are aware of the bid may be unfairly pressured into tendering their stock; and
— where takeover bids are made without any accompanying disclosure, target shareholders may not have sufficient information on which to weigh the merits of the bid.

Similar concerns were presented in the United States in the 1960s. They were a major factor in the 1968 enactment of the Williams Act.

III. TAKEOVER LAW IN AMERICA — A COMPARISON

A. *Overview — the Origins and Aims of the Williams Act*

Prior to the enactment of the Williams Act, there was no regulation of cash tender offers in the United States.[29] If, however, a company sought control of another by a stock-for-stock exchange, the offer was required to be registered under the Securities Act of 1933[30] and each shareholder was furnished with a prospectus containing all material facts about the offer. Where corporate control was sought through a proxy contest, section 14(a) of the Securities Exchange Act of 1934[31] required that shareholders be informed of the identity of the participants in the proxy contest, of their plans for the acquired company and certain other information.[32] In both the exchange offer and proxy contest, information was required to be filed with the Securities and Exchange Commission[32a] and both transactions were subject to statutory regulation.

In contrast, when a cash tender offer was made, no information was required to be filed or disclosed to shareholders. Since cash tender offers had a similar purpose to exchange offers and proxy contests, there appeared to be no justification for their exemption from the disclosure provisions of the securities laws. The gap was closed by the enactment of the Williams Act in 1968. The House of Representatives report on the Williams Act indicates that the Act's purpose was almost identical to that of New Zealand's 1963 amendment — neither to encourage nor discourage

29 "Tender offer" is the fetching title given to "takeover offers" in the United States.

30 15 U.S.C. ¶77a et seq., hereinafter referred to as the "Securities Act" or "1933 Act". The Securities Act is similar to New Zealand's Securities Act 1978 — both are primarily concerned with the insurance and sale of new securities. Indeed like its American equivalent, the New Zealand Securities Act would also require registration of a stock exchange offer.

31 15 U.S.C. ¶77b et seq., hereinafter referred to as the "Exchange Act" or "1934 Act". The Exchange Act focuses on the on-going regulation of the American securities markets and contains the Williams Act.

32 "Proxy contests" or "proxy fights", which have yet to catch on in the antipodes, are a popular method of seeking to gain control of a company in the United States.

32a The body charged with administering the 1933 and 1934 Acts, hereinafter referred to as the "SEC".

tender offers, but rather to ensure that shareholders have sufficient information to allow them to decide intelligently whether or not to tender their stock:[33]

> The Bill avoids tipping the balance of regulation either in favour of management or in favour of the person making the takeover bid. It is designed to require full and fair disclosure for the benefit of investors while at the same time providing the offeror and management equal opportunity to fairly present their case.

The report recognised that any possible discouragement of takeover activity was outweighed by the benefit of shareholder protection:[34]

> While the Bill may discourage tender offers or other attempts to acquire control by some who are unwilling to expose themselves to the light of disclosure, the committee believes this is a small price to pay for adequate investor protection. In fact, experience under the Securities Act of 1934 has amply demonstrated that the disclosure requirements of the federal securities acts are an aid to legitimate business transactions, not a hindrance.

Subsequent experience would seem to have borne out this prophecy. It has not been necessary to amend the Williams Act substantially during the fifteen-odd years it has been on the books. During that time, the expansion of the takeover phenomenon has continued almost exponentially. Thus, the American legislation appears to have established an effective arena for the sale of corporate control, without significantly impeding takeover activity.[35]

B. *The Legislative Scheme of the Williams Act and its Related Provisions*

The Williams Act is principally concerned with the regulation of tender offers and its central thrust is to ensure that adequate disclosure is made with enough time for shareholders to consider the merits of the bid on the basis of this information. Recognising, however, that changes in corporate control are often wrought by stock purchases on the open market, the Williams Act also attempts to ensure that adequate disclosure is made when this tactic is used.

The Williams Act is not, however, an isolated piece of legislation. It is supplemented by the general anti-fraud provisions of the federal securities laws, their general disclosure requirements and their proxy rules, to name only some of the more significant related provisions. Thus, among the most important observations to be made in this article are, first, that a takeover law should not be confined to the regulation of precise aspects of a takeover bid — it must be supplemented by the anti-fraud and general disclosure requirements of a general securities law. Secondly, the scope of a takeover law should not be confined to the formal tender offer situation — it should regulate other methods of gaining corporate control, such as creeping tender offers, "standing in the market" and proxy contests.

33 H.R. Rep. No. 1711, 90th Cong., 2d Sess. (1968) (the "Report"). See *Rondeau* v. *Mosinee Paper Corp.* 422 U.S. 49, 58-59 (1975).

34 Idem. Interestingly, the expressed purposes of the 1963 amendment to New Zealand's Companies Act were virtually identical. See the speech of the Hon. Mr. J. R. Hanan (Minister of Justice) in introducing the Bill on 24 September 1963, supra n.9; the speech of the Hon. Mr. J. R. Marshall (Minister of Industries and Commerce) at the committal of the Bill on 22 October 1963: N.Z. Parliamentary debates, vol. 337, 1963; 2654. See also the Commission's Review, vol. I, pp. 28-29.

35 See takeover statistics quoted in the Report of the SEC's Advisory Committee on Tender Offers (8 July 1983).

This section of the article, therefore, briefly describes the legislative machinery of the Williams Act and its related rules and regulations, demonstrating their effectiveness and their interdependence with many of the other provisions of the federal securities laws. Part of this section is devoted to defensive tactics and highlights the question as to whether some legislation on defensive techniques may be appropriate. In analysing the American legislation, comments will be interposed on its protential applicability in New Zealand.[36]

The Williams Act consists of sections 13(d), 13(e), 13(g), 14(d), 14(e) and 14(f) of the Exchange Act.[37] The two central provisions are section 13(d), which mandates the disclosure of beneficial ownership and other information following the acquisition of more than 5 per cent of any class of certain types of securities, and section 14(d), which regulates tender offers.[37a]

1. *Market and private purchases: section 13(d) and its related provisions*

Section 13(d) regulates private stock purchases which have a potential effect on corporate control.[38] It requires the revelation of the purchaser's purposes within ten days after he crosses the 5 per cent beneficial ownership threshhold of the target's stock.[39]

When triggered, section 13(d) mandates the filing of a schedule 13D[39a] with the SEC, the target and each stock exchange where the target's securities are traded. No distribution of the schedule 13D to the target's shareholders is required. The schedule is, however, publicly available and the American financial press invariably ensures maximum dissemination of the information in the schedule.

(a) the extent of section 13(d)'s application

Section 13(d) generally only applies to equity securities registered under section 12 of the Exchange Act. An issuer's stock must be registered under section 12 if the corporation is engaged in interstate commerce, its assets exceed $1,000,000 and its shares are held by more than 500 persons or if such securities are listed on a stock exchange.

36 Accordingly, in addition to existing legislation, the discussion will focus on the proposals for change contained in the Report of the Tender Offer Advisory Committee to the SEC, 8 July 1983, (hereinafter referred to as the "Advisory Committee Report"). The Advisory Committee was made up of experts in the takeover field.

37 Section 13(e) is not discussed because it relates to the issuer's repurchase of its own shares which is not permitted in New Zealand. See *Trevor* v. *Whitworth* (1887) 12 App. Cas. 409. Section 13(g) is not discussed either, as it relates to the specialised field of institutional investment. Section 14(f) is also not discussed since it concerns a narrow and specialised disclosure procedure for changes in the boards of directors of a company.

37a These provisions are reproduced in an Appendix to this article.

38 The Commission has suggested a law similar to s.13(d) in its proposed "Nominee Legislation".

39 The SEC has suggested legislation which would amend s.13(d) by requiring a filing immediately upon crossing the 5 per cent threshhold, so as to avoid large stock accumulations during the present "ten-day window" period.

39a The information required to be disclosed is summarised in (c) of this part of the article.

(b) disclosure threshhold

The section 13(d) disclosure threshhold was originally the acquisition of more than 10 per cent of the target's outstanding voting stock. It was lowered to 5 per cent in 1970. It should be noted that the lower the disclosure threshhold is, the earlier target management receives the warning that an acquirer is buying into its stock. This "early warning" factor directly ties into the chosen philosophy of a takeover law — a low disclosure threshhold favours incumbent management, while a high threshhold favours the acquirer, permitting him to establish a foothold before revealing motives. The question of where to impose the disclosure requirement is, therefore, one which requires balancing the competing interests of shareholders and insurgents.

The schedule 13D must be "promptly" amended if "any material change occurs in the facts set forth" therein.[40] Thus, the section 13(d) disclosure requirement is an on-going one. Accordingly, where an acquirer initially describes his purpose as "investment", he must file an amendment if he decides to go for control or to materially increase his holdings. There is a presumption that acquisitions or dispositions of 1 per cent or more of the target's securities are material for this purpose.[41]

(c) the section 13(d) disclosure requirements

The disclosure requirements imposed by section 13(d)(1) comprise:

- the identity and background of the purchaser and the nature of his beneficial ownership;
- the source and amount of the financing of the purchase;
- the purpose of the purchase, including specific details of the acquirer's plans for the target corporation if control is sought;
- the number of shares beneficially owned, including those the acquirer has the right to acquire; and
- any contracts or other arrangements the acquirer has with anyone relating to the target's shares.

Most section 13(d) litigation involves a challenge to the acquirer's section 13(d) disclosures. Typically, these challenges focus on the acquirer's purpose, charging that he has concealed his true intent to seek control of the issuer.[42]

Litigation challenging the veracity of section 13(d) disclosures underscores one problem with the section, which is that acquirers will often give the anti-

40 The concept of materiality is central to all federal securities laws but is not defined in the legislation itself. The classic definition of the term appears in *TSC Industries, Inc.* v. *Northway, Inc.* 426 U.S. 438, 449 (1976):

> An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote. . . . Put another way, there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the "total mix" of information available. (Footnote and citations omitted.)

41 See rule 13d-2(a).

42 Typically, s.13(d) litigation charges that the acquirer concealed his true intent to seek control of the evidence. See e.g. *Chromalloy American Corp.* v. *Sun Chemical Corp.* 611 F. 2d 240, 245-246 (8th Cir., 1979); *Kirsch Co.* v. *Bliss & Laughlin Industries, Inc.* 495 F. Supp. 488, 499 (W.D. Mich., 1980).

septic description of their purpose as mere "investment". Acquirers may only reveal their true purpose when their ownership position becomes so large as to be utterly inconsistent with an "investment" intention.[43] In two recent cases, however, the United States courts penalised such abuses of section 13(d) by ordering divestiture or rescission where stock was purchased under cover of such a blatantly false filing.[44]

(d) beneficial ownership

"Beneficial ownership" is a pivotal section 13(d) concept. The current definition is widely cast so as to prevent acquirers from concealing their purchases behind nominees, trusts and dummy companies. Beneficial ownership is also deemed to exist where there is a right to acquire shares within sixty days, for example by exercising an option to purchase.[45]

(e) groups

One of the problems that bedevils any takeover law is the situation where several acquirers band together to seize control of the target. Unless all their positions are disclosed and their unity is revealed, the target's shareholders may be deprived of the knowledge that control of their company is being threatened, since each individual group member's holding may be less than the disclosure threshhold. The SEC has attempted to solve this problem by requiring "group" disclosure. Accordingly, the rules promulgated under section 13(d) require a schedule 13D filing:[46]

> [W]hen two or more persons agree to act together for the purpose of acquiring holding voting or disposing of equity securities of an issuer, the group formed thereby shall be deemed to have acquired beneficial ownership, for purposes of section 13(d) and 13(g) of the Act, as of the date of such agreement, of all equity securities of that issuer beneficially owned by such persons.

United States courts have held that, although some type of agreement is necessary for a group to exist, the agreement need not be formal, nor need it be in writing.[47]

43 See *Dan River, Inc.* v. *Unitex Ltd.* 624 F. 2d 1216 (4th Cir., 1980), cert. denied, 449 U.S. 1101 (1981).

44 See *General Steel Industries, Inc.* v. *Walco National Corp.* [1981-1982] Fed. Sec. L. Rep. (CCH) ¶ 98, 402 (E.D. Mo., 1981); *Hanna Mining Co.* v. *Norcen Energy Resources Ltd.* [1982] Fed. Sec. L. Rep. (CCH) ¶ 98, 878 (N.D., Ohio, 1982); see also J. M. Tobin and J. J. Maiwurm "Beachhead Acquisitions: Creating Waves in the Market Place and Uncertainty in the Regulatory Framework" (1983) 38 Business Lawyer 419.

45 See rule 13d-3(a).

46 See rule 13d-5(b).

47 See e.g. *Wellman* v. *Dickinson* 682 F. 2d 355, 366 (2d Cir., 1982), cert. denied, 103 S. Ct. 1522 (1983); *Corenco Corporation* v. *Schiavone & Sons, Inc.* 362 F. Supp. 939 (S.D.N.Y.), aff'd, 488 F. 2d 207 (2d Cir., 1973); *Financial General Bankshares, Inc.* v. *Lance* [1978] Fed. Sec. L. Rep. (CCH) ¶ 96, 403 (D.D.C., 1978); *Mid-Continent Bancshares, Inc.* v. *O'Brien* [1982] Fed. Sec. L. Rep. (CCH) ¶ 98, 734 (E.D. Mo., 1982). The s.13(d) disclosure obligations are not confined to acquirers — they also apply to the target's incumbent management. Thus, a defensive management group owning more than 5 per cent of the target's stock may also have to file a Schedule 13D. See, e.g., *Jewelcor, Inc.* v. *Lafayette Radio Electronics Corp.* [1974-1975] Fed. Sec. L. Rep. (CCH) ¶ 95, 096 (S.D.N.Y., 1975); *Warner Communications Inc.* v. *Murdoch* Civ. No. 84-13 CMW (D. Del., 16 March 1984).

(f) a private right of action under section 13(d)

The Williams Act is silent as to whether there is any private right of action under the legislation. Nonetheless, a majority of the United States federal courts recognise that target companies and their shareholders have a private right of action for injunctions or other equitable relief under section 13(d).[48] A growing number of courts have, however, recently begun denying standing to seek injunctive relief under section 13(d).[49] Thus, the standing issue is an open question in the United States.

In the New Zealand context, it should be noted that permitting private litigants to sue would remove much of the enforcement burden from the shoulders of the government. On the other hand, permitting an unlimited private right of action for both the target and its shareholders might enable the legislation to be used as a weapon to stave off unwelcome control bids even when they do not violate substantive law. Whichever approach is deemed appropriate for New Zealand, it is submitted that express provision should be made for it — New Zealand will thereby avoid the uncertainty that is now plaguing the American securities community.

2. *Tender offers: section 14(d) and its related provisions*

Section 14(d) of the Exchange Act and the rules promulgated under it by the SEC regulate tender offers. They impose disclosure requirements on both the offeror and management of the target, and regulate the timing of the bid and certain aspects of its mechanics.

(a) the extent of section 14(d)'s application

Like section 13(d), section 14(d) generally applies only to securities registered under section 12 of the Exchange Act.[50] Section 14(d) regulates both tender offers for cash and "exchange" offers. If the offeror proposes to exchange debentures, its own shares or other securities as some or all of the consideration for the tendered securities, then the offer is called an exchange offer. Since they involve an issuance of securities, exchange offers generally have to be registered under the Securities Act.[51] These additional disclosure requirements are somewhat duplicative. The Advisory Committee recommends rationalising and co-ordinating this extra regulation, thereby treating exchange offers and cash offers "on an equal footing so that bidders, the market and shareholders" can decide between the two.[52]

48 See, e.g. *GAF Corp.* v. *Milstein* 453 F. 2d 709, 719-21 (2d Cir., 1971), cert. denied, 406 U.S. 910 (1972); *Computer Network Corp.* v. *Spohler* [1982] Fed. Sec. L. Rep. (CCH) ¶ 98, 623, at 93, 087 (D.D.C., 1981).

49 See, e.g. *Indiana National Corp.* v. *Rich* 554 F. Supp. 864, 873 (S.D. Ind., 1982); *Leff* v. *CIP Corp.* 540 F. Supp. 857, 863 (S.D. Ohio, 1982); *Gateway Industries, Inc.* v. *Agency Rent A Car, Inc.* 495 F. Supp. 92, 100-101 (N.D. Ill., 1980).

50 The offeror "person" is defined as an "individual, partnership, limited partnership, syndicate or other group [formed] for the purpose of acquiring, holding or disposing of the securities of an issuer.": s.14(d)(2); see Sec. Ex. Rel. No. 14692 (21 April 1978). Thus, the offeror definition is, potentially, as widely cast as the s.13(d) "group" concept.

51 See 15 U.S.C. §§ 77a-77aa.

52 See recommendation 5.

Section 14(d) only applies where, after consumation of the offer, the insurgent would be the beneficial owner of more than 5 per cent of the class of securities to which the offer applies. While preserving the 5 per cent minimum level, the Advisory Committee has recommended a major change to the extent of section 14(d)'s potential application:[53]

> No person may acquire voting securities of an issuer, if, immediately following such acquisition, such person would own more than 20% of the voting power of the outstanding voting securities of that issuer unless such purchase were made (i) from the issuer, or (ii) pursuant to a tender offer. The [SEC] should retain broad exemptive power with respect to this provision.

This recommendation was not adopted without extensive debate. Its essential purpose is to ensure that shareholders are given the maximum opportunity to participate in the tender offer process and to receive their share of any premium paid for the sale of corporate control.

Exactly what the judgment should be on takeovers by open market and private purchases is a complex question. A skilled practitioner of this type of acquisition could, in effect, gain control of a company without paying the premium that the securities markets generally require for a control position, all to the detriment of the shareholders in the company. On the other hand, this kind of buying activity provides liquidity for those shareholders prepared to sell at that particular point in time up to the amount the acquirer wishes to purchase. To force the acquirer to proceed by tender offer could, thus, impede flexibility in the acquisition process and discourage corporate takeovers.

(b) the definition of a tender offer

A formal, "conventional" tender offer is the primary focus of section 14(d):[54]

> The offer normally consists of a bid by an individual or group to buy shares of a company — usually at a price above the current market price. Those accepting the offer are said to tender their stock for purchase. The person making the offer obligates himself to purchase all or a specified portion of the tendered shares if certain specified conditions are met.

The Williams Act does not define the term "tender offer". The legislative history of the Act nevertheless makes it clear that it was intended to extend beyond orthodox tender offers to "open market or privately negotiated purchases of securities."[55] An eight-factor test has been applied by a number of United States courts in determining whether they were confronted by a tender offer.[56] The eight factors are:

53 See recommendation 14.

54 *Kennecott Copper Corp.* v. *Curtiss-Wright Corp.* 584 F. 2d 1195, 1206 (2nd Cir., 1978), quoting H.R. Rep. No. 1711, 90th Cong., 2d Sess., reprinted in [1968] U.S. Code Cong. & Ad. News 2811.

55 See remarks of Senator Williams, 113 Cong. Rec. 854, 856 (1967).

56 See, e.g., *Wellman* v. *Dickinson* 475 F. Supp. 783, 823-824 (S.D.N.Y., 1979), aff'd, 682 F. 2d 355 (2nd Cir., 1982), cert. denied, 103 S. Ct. 1522 (1983); *Brascan, Ltd.* v. *Edper Equities, Ltd.* 477 F. Supp. 773, 791 (S.D.N.Y., 1979); *Stromfeld* v. *Great Atlantic & Pacific Tea Co.* 484 F. Supp. 1264, 1272 (S.D.N.Y.), aff'd, 646 F. 2d 563 (2nd Cir., 1980); *In re Paine, Webber, Jackson & Curtis, Inc.* [1982-83] Fed. Sec. L. Rep. (CCH) ¶ 83, 310 (SEC Admin. Dec., 30 December 1982); *SEC* v. *Carter, Hawley, Hale Stores, Inc.* 587 F. Supp. 1248 (C.D. Cal., 1984).

— active and widespread solicitation of public shareholders for the shares of an issuer;
— solicitation made for a substantial percentage of the issuer's stock;
— offer to purchase made at a premium over the prevailing market price;
— terms of the offer are firm rather than negotiable;
— offer contingent on the tender of a fixed number of shares, often subject to a fixed maximum number to be purchased;
— offer open for only a limited period of time;
— offeree subjected to pressure to sell his stock;
— publicity preceding or accompanying the rapid accumulation of stock.

Stock acquisition programmes, consisting of open market purchases, privately negotiated transactions and other means of acquisition, have often been challenged as "tender offers". As a general rule, however, United States courts have been hesitant to hold that such transactions fall within the Williams Act.[57] For example, in the leading case on the open market purchase issue, the court held that there is no tender offer when all the purchaser does is:[58]

> . . . to acquire a large amount of stock in open market purchases, bidding cautiously so as to avoid bidding up the price of the stock to excessive levels unless there was large volume available at such prices.

On the other hand, as stated by the SEC:[59]

> To say that purchases take place on the floor of a securities exchange, however, does not end the inquiry. The use of facilities of an exchange may be a mere formality to disguise what is otherwise in effect a tender offer that should be subject to the requirements of the Williams Act.

The lack of definition of a tender offer in the American securities laws is truly a two-edged sword. On the one hand, allowing the courts to interpret the term freely permits flexibility in the enforcement of the Williams Act. On the other hand, the courts' unwillingness to extend the concept very far beyond the formal tender offer situation may ultimately demand a definition of the term so as to give the Williams Act greater effect by eliminating any uncertainty about its potential applicability.

The New Zealand legislature may well consider that defining a tender offer is

57 See, e.g., *Polinsky* v. *MCA, Inc.* 680 F. 2d 1286, 1291 (9th Cir., 1982); *LTV Corp.* v. *Grumman Corp.* 526 F. Supp. 106, 109-110 (E.D.N.Y., 1981); *Kennecott Copper Corp.* v. *Curtiss-Wright Corp.* 584 F. 2d 1195, 1206-1207 (2nd Cir., 1978).

58 *Brascan, Ltd.* v. *Edper Equities, Ltd.* 477 F. Supp. 773, 789 (S.D.N.Y., 1979).

59 Sec. Ex. Rel. No. 16385 (29 November 1979). It should be noted that the SEC has declared the "special bid" to be a tender offer under the Williams Act shortly after the Act became effective: Sec. Ex. Act Rel. No. 8392, at 2 (30 August 1968). As one commentator has described this acquisition process:
"The special bid is a stock market procedure designed to permit the purchase of blocks of securities too large to be readily handled in the regular auction market. A purchaser announces a special bid on the market tape, specifying the number of shares desired and a fixed bid price which is usually substantially higher than the concurrent market price. As sell orders are received on the floor, they are executed at once at the bid price, until the entire block has been acquired or the bid has been withdrawn." Note, "The Developing Meaning of 'Tender Offer' Under the Securities Exchange Act of 1934" (1973) 86 Harv. L.R. 1250, 1261. This tactic is strikingly similar to "standing in the market" in New Zealand.

essential in order to achieve certainty in the scope of its takeover law. It should be noted, however, that while the lack of a definition may cause uncertainty, an unduly restrictive definition will impede the remedial purposes of a takeover law, as the ease with which the 1963 amendment may be avoided demonstrates. One method of avoiding any definitional problem might be to have disclosure requirements trigger at certain acquisition levels (as occurs in Australia under the Companies (Acquisition of Shares) Act 1980). A middle ground on the definition question may be to leave the potential reach of the tender offer concept open but to specifically include such transactions as the formal bid and "standing in the market". Alternatively, or, in addition, the legislation could set forth a set of tests to be applied by the courts in determining whether a given situation is a tender offer.[59a]

(c) an overview of the disclosure and other requirements of section 14(d)

> Hostile tender offers are the high drama of Wall Street, but they have their tedious aspects. Chief among the latter is the vast amount of paper they generate, even before the offer is made. Offering and transmittal letters, newspaper announcements, and disclosure statements to be filed in Washington must be prepared before the offeror may invite tenders.[60]

Section 14(d) authorises the SEC to prescribe by rule the information which must be disclosed in tender offers. Under its rule-making power, the SEC has enacted a number of rules which regulate tender offers and prescribe the information which must be disclosed in connection with the offer.

(d) the offeror's disclosure and other obligations

The tender offer rules impose a number of substantive requirements upon offerors, many of which are similar to those set forth in the schedule to New Zealand's Companies Amendment Act 1963. Among the more important provisions of the tender offer rules are the following:

— offeror must file a schedule 14D-1. A bidder may not make a tender offer unless "as soon as practicable on the date of the commencement of the tender offer" it files a schedule 14D-1 with the SEC and hand delivers a copy of such schedule to the target company and any other bidder who has an offer outstanding.[61]

— the schedule 14D-1 contents. The section 14(d) disclosure requirements include and extend beyond those imposed by section 13(d). Among the more important facts the schedule 14D-1 must reveal are:
  — the bidder's identity and background;
  the source of the bidder's funds;
  the financial statements of the bidder if it is a corporation;
  — the bidder's plans for the target should the offer succeed.[62]

— the commencement of the offer. A tender offer commences when the offer is first published, sent or given to security holders. A tender offer must be commenced within five business days of the public announcement by the bidder of the identity of the bidder, the subject company and the number and class of shares sought and the offering price or prices, unless within five business days, the bidder withdraws the offer.[63]

59a See, e.g., the eight-factor test quoted supra n.56 and text. See also n.90 infra.

60 *United States* v. *Chiarella* 588 F. 2d 1358, 1362 (2nd Cir., 1978), rev'd, 445 U.S. 222 (1980).

61 Rule 14d-3(a).

62 See schedule 14D-1, items 2, 4 and 9.

63 Rules 14d-2(a), 14d-6.

— offer open for twenty days. An offer must remain open for twenty business days. An offer must also be open for ten business days after any increase in the offered consideration.[64]

— withdrawal rights. Security holders must be given the right to withdraw tendered shares during the first fifteen business days after commencement of the tender offer and, unless such shares have already been accepted for payment, for ten business days following commencement of a competing offer.[65]

— pro-ration period. Where the number of shares tendered is greater than the number of shares sought, the bidder must purchase on a pro rata basis from all security holders who tendered during the entire period the offer is open.[66]

— increased consideration. If the consideration offered is increased, the increased consideration must be paid to all tendering shareholders.[67]

(e) disclosure and other obligations of the target company

Several of the tender offer rules apply to the target company, many of these obligations are also similar to those in the 1963 amendment. Among the more important such rules are the following:

— target to facilitate dissemination of offer. The target company, at the written request of the bidder, must either mail and transmit to shareholders the bidder's tender offer materials or furnish its shareholders list to the bidder.[68]

— target must give statement of position. The target company must, within ten business days from the date the tender offer is first published, send or give to its security holders a statement of its position with respect to the offer or a statement why it cannot take a position.[69]

— target must file a Schedule 14D-9. The target company and its management, and various other persons, may not make a recommendation or solicitation with respect to the offer without filing as soon as practicable a schedule 14D-9 solicitation/recommendation statement with the SEC, the bidder and, where appropriate securities exchanges and the subject company as soon as practicable thereafter.[70]

— the schedule 14D-9 contents. Among the more important disclosure items in the target's solicitation recommendation statement are:[71]

  — a statement of the target's recommendations as to whether target shareholders should tender their stock and its reasons for its recommendation;

  — a statement as to whether there are any conflicts of interest arising out of any employment or other arrangements; and

  — "Whether or not any negotiation is being undertaken or is underway . . . in response to the tender offer" which relates to certain transactions, including negotiations with "white knights".

3. *The regulation of proxy solicitation: section 14(a) of the Exchange Act*

The solicitation of proxies for shareholder votes is a frequently used means of acquiring corporate control in the United States. The attractions of this method are its relative simplicity and generally lesser expense when compared to a tender offer. The proxy process usually involves seeking the proxies of target shareholders to vote at the target company's shareholders' meeting for a dissident

64 Rules 14e-1(a), 14e-1(b).
65 Section 14(d)(5), 14d-7.
66 Rule 14d-8.
67 Section 14(d)(7).
68 Rule 14d-5.
69 Rule 14e-2.
70 Rule 14d-9.
71 See schedule 14D-9, items 4 and 7. For a discussion of "white knights", see infra part 6(a).

slate of directors. As in New Zealand, state corporate law prohibits payment for a stockholder's vote. Stockholders are encouraged to vote for the dissidents in the same way as they are for rival politicians — by promises of improved management or perhaps even liquidation of the company and distribution of the proceeds among shareholders. It is not improbable that New Zealand will soon experience this method of seeking to gain corporate control by soliciting voters, given that the cash expenditure in seeking control by soliciting proxies is likely to be much less than in a tender offer. Therefore, it may be that New Zealand's takeover law should contain provisions regulating this method of gaining corporate control.

Section 14(a) of the Exchange Act and the rules promulgated under it regulate proxy solicitation. The primary purpose of this section is to protect the investor by preventing both incumbent management and the insurgents from obtaining proxies by means of deceptive or inadequate disclosure.

(a) the extent of section 14(a)'s application

Section 14(a) applies to any proxy solicitation directed to more than ten persons in respect of securities registered under section 12 of the Exchange Act. Thus, section 14(a) has, essentially, the same range as sections 13(d) and 14(a).

(b) the proxy rules

In the event of a contested election of directors, the proxy rules determine the ground rules within which the contest takes place. Among other things, they require the insurgents to file and use a proxy statement, and also to file a schedule 14B, both of which must be reviewed by the SEC prior to the dissemination of the proxy materials. The schedule 14B is broken into three sections which require disclosure of the following information:

— section 1: participants' identity and background. This section requires the following information about each participant in the proxy solicitation: his name; address; present and prior occupations; prior participation in proxy contests; and criminal convictions.

— section 2: participants' interest in issuer's securities. This section includes information with regard to: the amount of the company's securities owned; previous acquisitions of such securities; funds borrowed for such acquisitions; and agreements with other persons with regard to the company's securities.

— section 3: miscellaneous. This section requires a description of the circumstances under which the individual became a participant in the proxy contest; any material interest in transactions with the company; agreements with regard to future employment or transactions with the company; and the amount contributed or proposed to be contributed by the participant in furtherance of the proxy solicitation.

The proxy rules also provide a mechanism by which management must either furnish the insurgents with a shareholder list or mail their proxy material for them at the insurgent's expense. All subsequent proxy soliciting material — including advertisements, scripts for radio or television broadcasts, instructions to proxy solicitors, and the like — must also be filed with the SEC for a prescribed period of time prior to being used.

4. *The general disclosure requirements of the federal securities laws*

> The keystone of the entire structure of federal securities legislation is disclosure. Making available to investors adequate financial and other information about securities in which they might invest or have invested is the best means of enabling them to make intelligent investment decisions and of protecting them against securities frauds.[72]

Such information was historically provided by two principal disclosure systems: (a) disclosure under the Securities Act in connection with the public offering of securities, and (b) disclosure under the Exchange Act, on a continuous basis for companies with securities registered under either the 1933 or the 1934 Act.

The two systems often overlapped and produced disclosure duplications. This prompted the SEC to adopt an integrated disclosure system, the core of which is contained in regulation S-K. Regulation S-K provides a reservoir of all substantive data (other than financial statements[73]) required to be revealed under both the 1933 and the 1934 Acts. Some of the most important information items required to be disclosed under the regulation include:

— a description of the issuer's business;

— a description of the issuer's properties;

— disclosure of material pending legal proceedings against the issuer;

— markets in which the issuer's securities are traded together with dividend information;

— management's discussion and analysis of the financial statements including all relevant information with regard to the results of the issuer's operation, liquidity and capital resources; and

— disclosure concerning management and their positions in the company, including a description of transactions between management and the company, remuneration paid to management, interlocking directorships and security ownership of management and certain beneficial owners.

— security ownership of more than 5 per cent of any class of voting security.

The on-going disclosure requirements of the federal securities laws are provided for mainly in sections 13 and 14 of the Exchange Act. Section 13 to the Act requires a registered company to file with the SEC "Such Annual Reports . . . and such quarterly reports . . . as the SEC may prescribe." The basic reports required to be filed with the SEC under section 13 are:

— an annual report on form 10-K, which must be filed within ninety days after the end of the company's current fiscal year;

— a quarterly report on form 10-Q, filed within forty-five days of the end of the appropriate quarter for each quarter other than the year end quarter; and

— a current report on form 8-K for any month in which extraordinary events occur, such as major losses, which must be filed within fifteen days of the event.

72 Report of Special Study of Securities Markets by the Securities and Exchange Commission House document No. 95, 88th Cong. 1st Sess. Part 3, p. 1 (1933) (the "Special Study").

73 Financial statements are the subject of reg. S-X, the General Accounting regulation.

5. *The anti-fraud provisions of the federal securities laws*

The United States securities laws are supported by a wide range of anti-fraud provisions, including both general anti-fraud provisions such as section 17(a) of the 1933 Act and section 10(b) of the 1934 Act and takeover-specific provisions such as sections 14(e) and 14(a) of the 1934 Act. While the form of the anti-fraud provisions in the American securities laws might be improved upon, reflecting as it does their piecemeal development, their content and effectiveness is a significant illustration of the specific need for anti-fraud provisions in any takeover law, encompassing both civil and criminal penalties. Moreover, the questions that have arisen under the anti-fraud laws about private rights of action underscore the need for express legislation on this issue.

(a) section 17(a) of the 1933 Act

Section 17(a) of the Securities Act is a general anti-fraud provision which pertains to fraud in the sale or offer for sale of securities. Section 17(a) makes it unlawful to:

— make an untrue statement of a material fact;

— make a statement which is misleading because of the omission of a material fact;

— employ any device, scheme, or artifice to defraud; or

— engage in any practice which operates as a fraud or deceit.

Section 17(a) reflects the general pattern for defining fraud under the federal securities laws, but it is limited to the sale or offer for sale of securities. Significantly, the section is not limited in its application to large companies registered under section 12 of the 1934 Act. Rather, this general provision applies to all securities transactions, irrespective of the size of the issuer.[73a]

(b) section 10(b) of the 1934 Act

Section 10(b) of the Exchange Act is undoubtedly the most significant general anti-fraud provision of the United States federal securities laws. Section 10(b) makes it unlawful "in connection with the purchase or sale" of any security to use "any manipulative or deceptive device or contrivance" as defined by SEC regulations.

The SEC has adopted rule 10b-5 in 1943 pursuant to this section. The rule has become one of the most significant anti-fraud provisions in the United States securities laws and can be invoked by a shareholder who has sold his stock under a tender offer in reliance upon fraudulent disclosures. Rule 10b-5 defines fraud essentially in the same terms as section 17(a) of the Securities Act, making it unlawful:

— to employ any device, scheme, or artifice to defraud;

— to make any untrue statement of a material fact or omit to state a material fact

73a It is not clear whether there is a private right of action under s. 17(a). See *Aaron* v. *SEC* 446 U.S. 680 (1980). Unlike other circuits, the Second Circuit has held that there is a private right of action for purchasers under s. 17(a). See *Kirshner* v. *U.S.A.* 603 F. 2d 234, 241 (2nd Cir., 1978); *Adato* v. *Kagan* 599 F. 2d 1111, 1115 (2nd Cir., 1979).

necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or

— to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

While broader than section 17(a) in the sense that it is applicable to purchases as well as sales, section 10(b) and rule 10b-5 are narrower in the sense that they are not applicable to "offers".[74] Like section 17(a), section 10(b) and rule 10b-5 apply to all securities transactions — not just dealings in the shares of large companies.

(c) section 14(a) of the 1934 Act

Section 14(a) of the Exchange Act delegates to the SEC authority to regulate by rule the solicitation of proxies. Pursuant to this authority, the SEC has adopted rule 14a-9, a specific anti-fraud provision for proxy solicitation.[75] Rule 14a-9 makes it unlawful in connection with the solicitation of proxies to:

— make an untrue statement of material fact;

— make a statement which is misleading because of the omission of a material fact; or

— fail to correct an earlier statement which has become false or misleading.

(d) section 14(e) of the 1934 Act

Section 14(e) of the Exchange Act combats "fraud" by any person in connection with tender offers. "Fraud" is defined as:

— an untrue statement;

— a statement misleading because of the omission of a material fact; or

— engaging in any fraudulent, deceptive or manipulative acts or practices.[76]

6. *Takeover defensive techniques*

Most of the United States courts have held that target management have the right, if not the duty, to oppose any takeover bids they consider to be contrary to the interests of the target corporation and its shareholders.[77] It is well settled by the American courts that the state law fiduciary standard to which directors will be held in evaluating or opposing an unsolicited acquisition

74 For a comparison of ss. 17(a) and 10(b), see *Aaron* v. *SEC,* supra n.73a. The courts have recognised private rights of action under s. 10(b) but have not been so quick to do so under s. 17(a). See, e.g., *Herman & McLean* v. *Huddleston* 459 U.S. 375 (1983); *Aaron,* supra.

75 The United States Supreme Court has recognised a private right of action under s.14(a) and rule 14a-9: *J.I. Case Co.* v. *Borak* 377 U.S. 426 (1964).

76 The SEC has exercised its rule-making power under s.14(e) to regulate insider trading in the context of tender offers. See rule 14e-9. It should be noted that most courts have held that the target has an implied right of action to seek injunctive relief under ss.14(d) and (e) of the Williams Act. See, e.g., *Electronic Specialty Co.* v. *International Controls Corp.* 409 F. 2d 937 (2nd Cir., 1969); *Susquehanna Corp.* v. *Pan American Sulphur Co.* 423 F. 2d 1075 (5th Cir., 1970). The standing problems that have arisen under s.13(d) have not occurred under ss.14(d) and (e).

77 See, e.g., *Crouse-Hinds Co.* v. *Internorth, Inc.* 634 F. 2d 690, 702-704 (2nd Cir., 1980); *Berman* v. *Gerber Products Co.* 454 F. Supp. 1310, 1318 (W.D. Mich., 1978). Accord, rule 609 New Zealand Stock Exchange Rules.

proposal is the "business judgment rule". This rule requires directors to make their decisions in good faith and in accordance with what they reasonably believe to be in the best interests of shareholders. Absent a showing of fraud, self-dealing or bad faith, directors operate under a presumption of good faith and the burden of proof is on the party seeking to establish a failure to meet the business judgment standard.[78]

The SEC's Advisory Committee has defended the notion of the Common Law business judgment rule.[79] Nonetheless, the New Zealand legislature may consider that some legislative regulation of defensive tactics is appropriate in New Zealand's takeover law, both so as to reduce the uncertainty of the Common Law and in order to protect the minority shareholder. Indeed, the SEC's Advisory Committee has itself recognised that the interests of minority shareholders are sufficiently strong to warrant some regulation of defensive tactics. Set forth below are some of the more significant defensive techniques which have been used in the United States.

(a) white knights

Management of a takeover target often attempts to fight off a hostile bid by seeking a more palatable acquirer — a "white knight". Where such a "white knight" is found by a target, a "lock-up" arrangement is often entered into to secure his position. A "lock-up" generally involves an agreement giving the friendly acquirer some kind of control (by way of option or other contract, if not outright sale) over some of the target's shares or certain of its valuable assets. Such tactics discourage the hostile bidder from seeking to take over the target company because he might not then be able to acquire sufficient stock to seize control or, if assets are transferred, a successful bid might leave him with little better than an empty shell.

A "lock-up" has been held to be a manipulative device violating section 14(e) of the Exchange Act.[80] That decision has not, however, been accepted into the mainstream of tender offer law and a number of courts have declined to follow it, thus breathing new life into this defensive tactic.[81] The Advisory Committee does not suggest legislation on this defense — except to recommend that issuing more than 15 per cent of already outstanding securities to a white knight during a tender offer should have shareholder approval.[82]

78 See *Panter* v. *Marshall Field & Co.* 486 F. Supp. 1168 (N.D. Ill., 1980), aff'd, 646 F. 2d 271 (7th Cir.), cert. denied, 454 U.S. 1092 (1981); *Johnson* v. *Trueblood* 629 F. 2d 287 (3rd Cir., 1980), cert. denied, 450 U.S. 999 (1981); *Treadway Cos.* v. *Care Corp.* 638 F. 2d 357 (2nd Cir., 1981); *Norlin Corp.* v. *Rooney, Pace Inc.,* supra n.27a.

79 See recommendation 33.

80 See *Mobil Corp.* v. *Marathon Oil Co.* 669 F. 2d 366, 375-376 (6th Cir., 1981).

81 See *Marshall Field & Co.* v. *Icahn* 537 F. Supp. 413, 420-422 (S.D.N.Y., 1982); *Buffalo Forge Co.* v. *Ogden Corp.* 717 F. 2d 757, 759-780 (2nd Cir.), cert. denied, 104 S. Ct. 550 (1983).

82 See recommendations 41 and 42. It should be noted that the SEC has proposed legislation on this point: see infra. In addition, N.Z. Stock Exchange rule 425(2) prohibits stock issuance above the 10 per cent level without stockholder approval.

It is submitted that the same type of limitation should apply to asset sales, which have a substantially identical effect — the discouragement of a hostile bid. Thus, it is submitted, a takeover law should also require shareholder approval where during a tender offer more than 15 per cent of the target's assets are transferred to a friendly third party. Such provisions would not unduly restrict the target company's freedom to contract since they would only apply during a tender offer. Moreover, such a restriction could prevent incumbent management from imposing its will on the target company's shareholders by making the tender offer futile.

(b) counter-offers

American tender offer targets have recently begun using the "pac-man" defense — a counter tender offer for the hostile bidder. This tactic was used by New Zealand Forest Products Ltd. in attempting to stave off a hostile takeover bid by New Zealand's Wattie Industries Ltd.[83] The best known American example of this tactic occurred when Martin Marietta made a tender for Bendix in response to the Bendix tender offer for Martin Marietta. The pac-man defense, though expensive, proved successful — Martin Marietta remained independent. Moreover, in the course of the battle for control, the legality of the pac-man defense was upheld by the courts.[84]

Any neutral takeover law would obviously encompass a pac-man bid in the same way that it regulates the original tender offer. Thus, extensive special legislation on this point is neither necessary nor appropriate. It should be noted, however, that while the SEC's Advisory Committee recommends "no general restrictions on the counter tender offer as a defense", it is of the opinion that they should be prohibited where the original offer is in cash and is for 100 per cent of the target's stock.[85] The philosophy of this suggestion is that to permit target management to mount a counter offer against a 100 per cent bid would enable them to use the defense purely for their own purposes which would be an abuse of their fiduciary position.

(c) shark repellant provisions

Corporations which consider themselves as potential takeover targets often adopt "shark repellant" provisions in their charter or by-laws. Such arrangements include:

— classified board of directors. A classified board of directors is divided into classes which serve staggered terms. This structure makes it impossible to unseat the entire board at once.

— supermajority provision. This is a charter or by-law provision requiring a greater affirmative vote than required by state company law. Such provisions are applied to transactions resulting in changes in corporate control that require shareholder approval. They erect a higher than normal hurdle to a potential acquirer.

83 See *N.Z. Forest Products Limited* v. *New Zealand Stock Exchange,* supra n.27.
84 See *Martin Marietta Corp.* v. *Bendix Corp.* 549 F. Supp. 623, 627-628 (D. Md., 1982). See also *Buffalo Forge Co.* v. *Ogden Corp.,* supra n.81; *Dan River, Inc.* v. *Icahn* [1982-1983] Fed. Sec. L. Rep. ¶ 99, 043 (4th Cir., 1983).
85 See recommendation 40.

— "golden parachutes". These generally involve substantial payments of some kind to key executives who may lose their jobs as a result of a change in corporate control.

— employment contracts. The jobs of target management may be protected by long-term employment contracts. This has the effect of discouraging takeovers since it complicates the unseating of the incumbents.

— "poison pills". These are effected by the target issuing preferred stock with the right of conversion into shares of the acquirer should a successful tender offer be made, or alternatively, providing for mandatory redemption using the target's funds.

The SEC Advisory Committee is highly critical of shark-repellant provisions. Indeed, it has recommended their prohibition where they erect unduly high barriers to changes in corporate control.[86] To the extent not prohibited, the Committee has recommended legislation to require ratification of such provisions by shareholders every three years. The Committee has also recommended that target management should be prohibited from adopting "golden parachutes" and other shark repellants after a takeover bid has commenced and that such arrangements should be regularly disclosed by the issuer.[87] The New Zealand legislature may consider that some legislation along these lines may be appropriate, so as to prevent target management from abusing the defensive tactics that are available to them.

IV. CONCLUSION: A POSSIBLE LEGISLATIVE FRAMEWORK FOR A NEW ZEALAND TAKEOVER CODE

Both structural and substantive guidelines for a New Zealand takeover law may be derived from the Williams Act. Some of the problems that have arisen with the American legislation are also helpful in signposting pitfalls that New Zealand may avoid — problems such as the question of standing to sue, undue regulatory complexity and the abuse of defensive tactics. A caveat should, however, be raised in terms of structure — the Williams Act was superimposed upon a highly developed existing scheme of regular corporate disclosure and anti-fraud provisions. If the American experience is any indication, it seems clear that a takeover code cannot function in isolation — it should be supported by general disclosure and anti-fraud provisions, such as those contained in the 1934 Act.

Set forth below are some legislative concepts that may be distilled from the Williams Act, which might be helpful in New Zealand:

1. *Coverage of the legislation.* (a) The legislation should specify whether or not it extends only to public companies traded on the New Zealand Stock Exchange; (b) the legislation should govern the following methods of acquiring corporate control: market purchases; tender offers, including "standing in the market"; and proxy contests.[88]

86 See recommendation 35. Legislation restricting these defensive techniques has recently been introduced in Congress. In addition, the recently enacted Tax Reform Act of 1984 imposes a penal tax on excessive "golden parachute" payments. Such contracts are already regulated in New Zealand under ss. 191-194 of the Companies Act.

87 See recommendation 38.

88 The Commission has proposed "nominee legislation", regulating market purchases which is similar to s.13(d). A code regulating takeovers has also been proposed by the Commission in its Review, Chapter 7. There is, currently, no proposal for legislation regulating proxy contests.

2. *Market purchases.* A section 13(d) equivalent should be enacted as part of the code, triggering disclosure of both purchases and purposes when a certain percentage of the target's voting securities are acquired.[89]
3. *Takeover bids.* At the core of the code should be a scheme regulating takeover bids, but only so far as to ensure target shareholders receive adequate time and information to consider the bid. Care should be taken to formulate a definition of a "takeover" that is wide enough to make the code meaningful and which specifically includes such tactics as "standing in the market".[90]
4. *Proxy contests.* Provision should be made for the regulation of the acquisition of control through proxy solicitation, primarily by mandating the disclosure of material information about the person soliciting the proxies.
5. *Defensive tactics.* Some regulation of defensive tactics may be necessary to prevent their abuse and to avoid the uncertainties of the existing Common Law.
6. *Periodic disclosure.* The takeover code should be supported by requirements for regular disclosure made by public companies.
7. *Regulatory flexibility.* Given rapidity with which new takeover techniques are developed, effective regulation may best be achieved by enacting a general legislative framework on which more specific rulemaking by New Zealand's Securities Commission may be based. This is what is done by the SEC in the United States.
8. *Anti-fraud provisions.* The regulation of insider trading, false and misleading statements and market manipulation is an essential support to any takeover code.
9. *Private rights of action enforcement.* (a) If private rights of action under the code are deemed appropriate, they should be expressly granted, the range of civil relief available should be defined and statutes of limitation should be established; (b) provision for enforcement by the government and/or the Commission should be made, defining criminal and civil penalties, including injunctive relief.

Inclusion of such provisions in a takeover law would help to ensure that New Zealand benefits from the example and lessons of the comprehensive system of takeover legislation in the United States, and would assist the New Zealand legislature to fashion legislation best suited to New Zealand's particular needs and concerns.

89 The Commission's proposed "nominee legislation" is similar to s.13(d) and would satisfy this need.

90 The Commission proposes a takeover code which would avoid any definitional problem by triggering at certain percentage levels. The first problem with this scheme is that it only applies to purchases above the 20 per cent level so that pressure tactics could still be used below that level, yielding a sizeable foothold in the target company. Secondly, a code which imposes regulation on any purchase above the 20 per cent level may be too restrictive, thus impeding the takeover process. It is submitted that the better approach is to formulate a careful definition of a takeover and limit the application of the code to transactions that fall within that formulation.

APPENDIX

PROVISIONS OF THE WILLIAMS ACT

Section 13(d)

(1) Any person who, after acquiring directly or indirectly the beneficial ownership of any equity security of a class which is registered pursuant to section 12 of this title, or any equity security of an insurance company which would have been required to be so registered except for the exemption contained in section 12(g)(2)(G) of this title, or any equity security issued by a closed-end investment company registered under the Investment Company Act of 1940, is directly or indirectly the beneficial owner of more than 5 per centum of such class shall, within ten days after such acquisition, send to the issuer of the security at its principal executive office, by registered or certified mail sent to each exchange where the security is traded and file with the Commission, a statement containing such of the following information, and such additional information, as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors—

(a) the background, and identity, residence, and citizenship of, and the nature of such beneficial ownership by, such person and all other persons by whom or on whose behalf the purchases have been or are to be effected;

(b) the source and amount of the funds or other consideration used or to be used in making the purchases, and if any part of the purchase price is represented or is to be represented by funds or other consideration borrowed or otherwise obtained for the purpose of acquiring, holding, or trading such security, a description of the transaction and the names of the parties thereto, except that where a source of funds is a loan made in the ordinary course of business by a bank, as defined in section 3(a)(6) of this title, if the person filing such statement so requests, the name of the bank shall not be made available to the public;

(c) if the purpose of the purchases or prospective purchases is to acquire control of the business of the issuer of the securities, any plans or proposals which such persons may have to liquidate such issuer, to sell its assets to or merge it with any other persons, or to make any other major change in its business or corporate structure;

(d) the number of shares of such security which are beneficially owned, and the number of shares concerning which there is a right to acquire, directly or indirectly, by (i) such person, and (ii) by each associate of such person, giving the background, identity, residence, and citizenship of each such associate; and

(e) information as to any contracts, arrangements, or understandings with any person with respect to any securities of the issuer, including but not limited to transfer of any of the securities, joint ventures, loan or option arrangements, puts or calls, guarantees of loans, guarantees against loss or guarantees of profits, division of losses or profits, or the giving or withholding of proxies, naming the persons with whom such contracts, arrangements, or understandings have been entered into, and giving the details thereof.

(2) If any material change occurs in the facts set forth in the statements to the issuer and the exchange, and in the statement filed with the Commission, an amendment shall be transmitted to the issuer and the exchange and shall be filed with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(3) When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a "person" for the purposes of this subsection.

* * *

Section 14(d)

(1) It shall be unlawful for any person, directly or indirectly, by use of the mails or by any means or instrumentality of interstate commerce or of any facility of a national securities exchange or otherwise, to make a tender offer for, or a request or invitation for

tenders of, any class of any equity security which is registered pursuant to section 12 of this title, or any equity security of an insurance company which would have been required to be so registered except for the exemption contained in section 12(g)(2)(G) of this title, or any equity security issued by a closed-end investment company registered under the Investment Company Act of 1940, if, after consummation thereof, such person would, directly or indirectly, be the beneficial owner of more than 5 per centum of such class, unless at the time copies of the offer or request or invitation are first published or sent or given to security holders such person has filed with the Commission a statement containing such of the information specified in section 13(d) of this title, and such additional information as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors. All requests or invitations for tenders or advertisements making a tender offer or requesting or inviting tenders of such a security shall be filed as a part of such statement and shall contain such of the information contained in such statement as the Commission may by rules and regulations prescribe. Copies of any additional material soliciting or requesting such tender offers subsequent to the initial solicitation or request shall contain such information as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors, and shall be filed with the Commission not later than the time copies of such material are first published or sent or given to security holders. Copies of all statements, in the form in which such material is furnished to security holders and the Commission, shall be sent to the issuer not later than the date such material is first published or sent or given to any security holders.

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