

Indiana Law Review

Volume 21

1988

Number 1

Developments in Business Associations Law: CTS Corporation v. Dynamics Corporation of America

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There is definitely something to be said for persistence. Since 1975, Indiana, like a majority of states, has attempted to limit if not outright stop hostile corporate takeover attempts.¹ Most early state efforts to regulate hostile takeover attempts were blatantly pro-management and anti-offeror. As a result they were subject to serious constitutional challenge on two grounds: (1) they imposed an impermissible burden on interstate commerce and violated the commerce clause of the constitution,² or (2) they conflicted with the balanced approach to takeovers reflected in the Williams Act amendments³ to the Securities Exchange Act of 1934⁴ and were preempted by the federal statute under the supremacy clause.⁵

One of the earliest cases to consider the constitutionality of a state antitakeover statute invalidated the Idaho Business Takeover Act⁶ on both grounds.⁷ However, when that case reached the United States

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¹IND. CODE §§ 23-2-3-1 to -12 (West Supp. 1975) (repealed 1979). The first Indiana Business Takeover Law was discussed in Galanti, *Business Associations, 1975 Survey of Recent Developments in Indiana Law*, 9 IND. L. REV. 33, 52-59 (1975) and Note, *The Indiana Business Takeover Act*, 51 IND. L. J. 1051 (1976).

²U.S. CONST. art. I § 8, cl. 3.

³15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1982).

⁴15 U.S.C. § 78 (1982).

⁵U.S. CONST. art. VI, cl. 2.

⁶IDAHO CODE §§ 30-1501 to -1513 (Supp. 1979).

⁷*Great W. United Corp. v. Kidwell*, 439 F. Supp. 420 (N.D. Tex. 1971), *aff'd* 577 F.2d 1256 (5th Cir. 1978), *rev'd on other grounds sub nom. Leroy v. Great W. United Corp.* 443 U.S. 173 (1979).

Supreme Court⁸ the Court did not reach the merits of the dispute. Rather it reversed because venue to challenge the validity of the Idaho statute as applied to an Idaho corporation was improper in the United States District Court for the Northern District of Texas.⁹

The Supreme Court eventually reached the merits of the first generation of state antitakeover statutes in *Edgar v. MITE Corp.*¹⁰ In *MITE*, the Court held the Illinois Business Takeover Act¹¹ violated the commerce clause by placing an excessive indirect burden on interstate commerce. A plurality of the Court held that the Illinois act also violated the commerce clause by imposing a direct burden on interstate commerce.¹² Three justices thought the state law was preempted by the Williams Act.¹³

The rationale behind striking down the Illinois Act for imposing an improper indirect burden on commerce was that protecting shareholders, the avowed purpose of the statute, did not justify regulating tender offers to shareholders residing outside Illinois. In fact, the scheme of the Illinois Act could harm those shareholders because the delays permitted by the statute could help management defeat value increasing tender offers.¹⁴

The four justice plurality in *MITE* reasoned that the Illinois Act, by its terms, could have applied to tender offers in which no shareholder of the target company was a resident of Illinois. They also noted that if such statutes were adopted across the country, "interstate commerce in securities transactions generated by tender offers would be thoroughly stifled."¹⁵

The three justices,¹⁶ who urged that the Williams Act amendments to the Securities Exchange Act of 1934 preempted the Illinois Business

⁸*Leroy v. Great W. United Corp.*, 443 U.S. 173 (1979).

⁹*Great Western*, 443 U.S. at 186-87.

¹⁰457 U.S. 624 (1982).

¹¹ILL. REV. STAT. ch.121 1/2, § 137.51 (1979).

¹²*MITE*, 457 U.S. at 641-43.

¹³*Id.* at 630-39. Justice White was joined by Chief Justice Burger and Justice Blackmun on this issue. Three justices believed the case was moot, *id.* at 655-64 (Marshall, J., dissenting), and one believed that it failed to present a justiciable controversy. *Id.* at 664-67 (Rehnquist, J., dissenting).

¹⁴*Id.* at 644. See generally Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161, 1174-82 (1981).

¹⁵*MITE*, 457 U.S. at 642 (White, J., Burger, C.J., Powell and O'Connor, J.J.). The original Indiana Takeover Act, IND. CODE §§ 23-2-3-1 to -12 (West Supp. 1975) (repealed 1979) also had such extraterritorial scope. *Id.* § 23-2-3-1(j). See Galanti, *Corporations, 1979 Survey of Recent Developments in Indiana Law*, 13 IND. L. REV. 133, 161-72 (1980); Galanti, *Business Associations, 1975 Survey of Recent Developments in Indiana Law*, 9 IND. L. REV. 33, 53-59 (1975); Note, *The Indiana Business Takeover Act*, 51 IND. L.J. 1051 (1976).

¹⁶*MITE*, 457 U.S. at 630-34 (White, J., Burger, C.J. and Blackmun, J.).

Takeover Act, accepted the fact that the Exchange Act itself permits states to regulate securities as long as the regulations do not conflict with the Act itself.¹⁷ They also recognized that it was possible for a tender offer to comply with both federal and state law. However, Justice White argued the Illinois statute frustrated the two primary objectives of the Williams Act: shareholder protection and a balancing of the interests of management, offerors, and targets.¹⁸ "Congress sought to protect the investor not only by furnishing him with the necessary information but also by withholding from management . . . any undue advantage that could frustrate the exercise of an informed choice."¹⁹ In other words, the intent of the Williams Act was to establish a level playing field²⁰ and any state effort to "tilt" the balance towards management had to fall under the supremacy clause.²¹

The original Indiana Business Takeover Act was superseded in 1979 by the Indiana Takeover Offers Act.²² The constitutionality of this statute never has been resolved completely. The validity of the statute was challenged in *City Investing v. Simcox*.²³ The court purportedly abstained from deciding the validity issue because there was some question whether the purchase of shares by the plaintiff was a takeover offer within the meaning of the act. Under the so-called *Pullman* abstention doctrine originally articulated by Justice Frankfurter in *Railroad Commission v. Pullman*²⁴ federal courts will refrain from prematurely deciding constitutional issues pending determination in state courts of state law issues central to the constitutional dispute.²⁵

As courts are sometimes wont to do, after determining it did not have to resolve plaintiff's challenge in the Takeover Offers Act, the District Court in *Simcox* went to the "merits" and held the statute was valid. The court, however, only reached conclusions and did not discuss to any great extent the constitutional grounds for invalidating state

¹⁷*MITE* 457 U.S. at 630-31 (citing 15 U.S.C. § 78bb(a) (1982)).

¹⁸*MITE*, 457 U.S. at 631-34.

¹⁹*Id.* at 634.

²⁰See *Piper v. Chris-Craft Indus.*, 430 U.S. 1, 26-34 (1977).

²¹*MITE*, 457 U.S. at 632-34.

²²IND. CODE §§ 23-2-3.1-1 to -11 (Supp. 1987). See Galanti, *Corporations, 1979 Survey of Recent Developments in Indiana Law*, 13 IND. L. REV. 133, 161-72 (1980).

²³476 F. Supp. 112 (S.D. Ind. 1979), *aff'd*, 633 F.2d 56 (7th Cir. 1980).

²⁴312 U.S. 496 (1941).

²⁵*Id.* See *Moore v. Sims*, 442 U.S. 415 (1979). There are two other species of abstention in addition to *Pullman* abstention: (1) *Burford* abstention where federal courts relegate federal issues to state courts because those issues touch matters of traditional state concern, see *Burford v. Sun Oil Co.*, 319 U.S. 315, 317-18 (1943); and (2) *Younger* abstention where federal courts abstain from interfering with state criminal prosecutions out of deference for state functions. See *Younger v. Hams*, 401 U.S. 37, 44 (1971).

antitakeover statutes raised in *Great Western* and *MITE*.²⁶ The decision in *Simcox* was affirmed by the Seventh Circuit on the basis of the *Pullman* doctrine²⁷ without getting to the merits.²⁸

The wisdom of the Seventh Circuit in *Simcox* was borne out by the Indiana Court of Appeals in *In re City Investing Co.*²⁹ when it reversed the Indiana Securities Commissioner's cease and desist order against the offeror. As anticipated by the Seventh Circuit, the Indiana court concluded the purchase of the target's shares was not a takeover offer within the meaning of the Act.³⁰ The court rejected the state's contention that the Takeover Offers Act was intended to regulate all shifts in corporate control through stock purchases, and not just tender offers, as being "overbroad and contrary to the plain language of the Act."³¹ A "takeover offer" is not limited to conventional tender offers, but the term has an established legal significance. The court presumed that the legislature intended the term to be given its customary legal meaning in the Act absent any indication to the contrary.³² The definition of takeover offers in the Takeover Offers Act is similar to that found in section 14(d) of the Williams Act.³³ Consequently, the *City Investing* court concluded that takeover offers regulated by the Indiana Act are those offers to acquire the equity securities of "a company pursuant to that which is regulated by the Williams Act"³⁴

There was a shift away from using blunderbuss antitakeover statutes typified by the Illinois statute invalidated in *MITE* in the early 1980's. Because those statutes attacked the tender offer itself they invited challenge on Williams Act preemption and commerce clause grounds. Those concerned with hostile takeovers realized that the primary concern of antitakeover statutes should be the interests of shareholders because it is they who stand to lose if "unfair" tender offer practices continue.³⁵

²⁶476 F. Supp. at 115.

²⁷633 F.2d 56, 60 (7th Cir. 1980).

²⁸However, there was little doubt as to the Seventh Circuit's view on the merits. On the same day *Simcox* was decided the court invalidated the Illinois Business Takeover Act in *MITE Corp. v. Dixon*, 633 F.2d 496 (1980), *aff'd sub nom. Edgar v. MITE Corp.*, 457 U.S. 624 (1982).

²⁹411 N.E.2d 420 (Ind. Ct. App. 1980).

³⁰*Id.* at 432.

³¹*Id.* at 426.

³²*Id.* at 427.

³³15 U.S.C. § 78n(d)(1) (1982).

³⁴*City Investing*, 411 N.E.2d at 427.

³⁵Concerned parties include management of potential target companies, fearful of losing jobs, and state and local officials fearful of losing corporate home offices to other states. These are certainly legitimate concerns. Whether they should stand in the way of a free market for corporate control is an entirely different matter. Others are simply

Of course, it is also the shareholders who stand to lose if management is able to thwart a tender offer carrying a premium over the then market price of the target's shares.

Thus the focus of antitakeover efforts began to shift. Changes were made to existing antitakeover statutes ranging from self-serving statements that the purpose of the statute is to ensure that shareholders can make an "informed and well-reasoned investment decision"³⁶ to provisions requiring takeover offers to be made to all shareholder-offerees of the same class on substantially equivalent terms³⁷ to provisions limiting subsequent acquisition of equity securities by an offeror following the conclusion of a takeover offer.³⁸

Current efforts to block hostile takeover attempts also are found in general corporation statutes. For example, the Indiana Business Corporation Law³⁹ contains two chapters intended to regulate "change of control transactions": the Control Share Acquisition Chapter⁴⁰ and the Business Combinations Chapter.⁴¹

The Control Share Acquisition Chapter does not on its face prohibit the acquisition of shares either pursuant to a tender offer or in market transactions. Rather it limits the voting rights of such shares unless independent shareholders, (shareholders other than the acquiring shareholder, an officer of the target company or an employee-director of the target company),⁴² adopt a resolution granting the right to vote to the bidder.⁴³ The statutory provisions are triggered whenever a person acquires shares that raise total holdings over a "control share" threshold—20, 33 1/3, or 50 percent of outstanding shares.⁴⁴ The acquiring shareholder can request management of the target company to submit to the shareholders within fifty days the issue of the right of the acquiring shareholder

troubled by the practices and financing methods used by persons and companies aggressively active in the tender offer "game," "corporate raiders" as it were. These, too, are certainly legitimate concerns. Whether they should be addressed at the state level where theoretically 50 different rules can apply to a tender offer or at the federal level because the companies affected as offerors or targets will have facilities and shareholders in many states also is an entirely different matter.

³⁶This provision was added to the Indiana Business Takeover Offers Act in 1981. IND. CODE § 23-2-3.1-0.5(b) (Supp. 1987).

³⁷This provision was added to the Indiana Business Takeover Offers Act in 1983. See IND. CODE § 23-2-3.1-6-5 (Supp. 1987).

³⁸*Id.*

³⁹IND. CODE §§ 23-1-17-1 to -54-2 (Supp. 1987).

⁴⁰IND. CODE §§ 23-1-42-1 to -11 (Supp. 1987).

⁴¹IND. CODE §§ 23-1-43-1 to -24 (Supp. 1987).

⁴²See IND. CODE § 23-1-42-3 (Supp. 1987). Outside directors of the target company are considered "non-interested" under the statute.

⁴³*Id.* 23-1-42-9.

⁴⁴IND. CODE § 23-1-43-1 (Supp. 1987).

to vote the acquired shares.⁴⁵ If no request for a special meeting is made, the issue of voting rights is considered at the next special or annual shareholder meeting.⁴⁶

If authority existed in the target's articles of incorporation or bylaws in advance of the control share acquisition, and the acquiring shareholder does not timely file an acquiring person's statement, the target can redeem at a fair value the shares acquired within a period of sixty days following the last acquisition of shares.⁴⁷ If the acquiring shareholder makes a request for a meeting, its shares can only be redeemed in the event that the independent shareholders deny full voting rights.⁴⁸ If the shareholders grant the bidder full voting rights and the acquiring shareholder has thereby acquired a majority of all voting power, shareholders who have exercised dissenters' rights of appraisal can receive fair value of their shares.⁴⁹

The Business Combinations Chapter of the Indiana Business Corporation Law (IBCL)⁵⁰ purports to protect unsophisticated investors, as compared to sophisticated investors such as arbitragers, from the undesirable effects of a hostile tender offer. These effects result from either tendering too quickly and not getting the full benefits of the offer or not tendering at all and being the victim of an unfair "freeze out" at the end of a successful takeover.⁵¹

Under the Business Combinations Chapter an offeror who has acquired in excess of ten percent of the outstanding voting securities of a "resident domestic corporation" or any subsidiary⁵² is prohibited from engaging in a merger or any of an enumerated list of transactions with the target company⁵³ for a period of five years following the acquisition

⁴⁵IND. CODE § 23-1-42-7(b) (Supp. 1987). The acquiring shareholder must give an undertaking to pay the expenses of the special meeting. *Id.* § 23-1-42-7(a).

⁴⁶IND. CODE § 23-1-4-7(c) (Supp. 1987).

⁴⁷IND. CODE § 23-1-42-10(a) (Supp. 1987). The chapter defines "fair value" as a value not less than the highest price paid per share by the acquiring person in the control share acquisition. *Id.* § 23-1-42-11(c).

⁴⁸*Id.* § 23-1-42-10(b).

⁴⁹*Id.* § 23-1-42-11.

⁵⁰*Id.* § 23-1-43-1 to -24.

⁵¹See Strain, *Provisions Affecting Change of Control Transactions in the New Indiana Business Corporation Law*, ICLEF NEW INDIANA BUSINESS CORPORATION LAW SEMINAR VII-4 to VII-7 (1986). It is interesting to note that the drafters of antitakeover legislation such as that found in the IBCL tend to think in terms of unfair freezeouts by hostile tender offerors and ignore the possibility of unfair freezeouts by management leveraged buy outs.

⁵²IND. CODE § 23-1-43-10(a) (Supp. 1987). A resident domestic corporation is defined as "a corporation that has one hundred (100) or more shareholders." *Id.* § 23-1-43-13(a). A resident domestic corporation does not cease to be one because of events occurring or actions taken while subject to the chapter. *Id.* § 23-1-43-13(b).

⁵³*Id.* § 23-1-43-5.

of the shares.⁵⁴ After that time, a transaction can occur if it either results in a fair price to the independent shareholders, as defined in the statute, or is done pursuant to the affirmative vote of a majority of the independent shareholders.⁵⁵

Interestingly, the five year delay does not apply if the business combination or the purchase of shares made by the acquiring shareholder is approved by the board of directors of the corporation before the shares are acquired.⁵⁶ Equally interesting, business combinations approved by the board of directors of the corporation before the shares are acquired or implemented by means of shares acquired with the prior approval of the board of directors are permitted without a vote of a majority of the independent shareholders and without satisfying the fair price requirement.⁵⁷ In other words, deals favored by management are exempt regardless of their impact on shareholders.

The consideration to which shareholders of the target are entitled is the highest price paid by the acquiror for the shares that gave rise to the control position plus an interest add-on over the period tied to the one-year treasury bill rate.⁵⁸ Theoretically this gives shareholders of Indiana corporations the option of riding with the new owners, knowing in advance what their floor will be at the end of five years. Those who otherwise would have been frozen out for paper or something less than fair consideration for their shares are protected.⁵⁹ Unless, of course, it is a deal favored by management. A favored deal may bring the highest price to shareholders⁶⁰ but that depends on the sincerity of management's interest in shareholders as opposed to their interest in their own jobs.⁶¹

The adoption of the Business Combinations chapter was such a high priority of the 1986 session of the General Assembly that it received the honor of being Senate Bill No. 162 as well as being chapter 43 of the later enacted IBCL. It became effective on January 23, 1986, and applied to Indiana corporations unless they "opted" out by an amendment to the corporation's by-laws by February 1, 1986.⁶³ The Business

⁵⁴*Id.* § 23-1-43-18(a).

⁵⁵*Id.* § 23-1-43-19(2).

⁵⁶*Id.* § 23-1-43-18(a).

⁵⁷*Id.* § 23-1-43-19(1).

⁵⁸*Id.* § 23-1-43-19(3).

⁵⁹See Strain, *supra* note 51, at VII-5, VII-6.

⁶⁰*Id.* at VII-6.

⁶¹History shows that management of target companies acquired in a hostile takeover do not remain employed by the target for very long.

⁶²IND. CODE § 23-2-9-1 to -22 (Supp. 1986). This statute was repealed effective August 1, 1987, which was the effective date of the IBCL.

⁶³IND. CODE § 23-3-9-22(3)(B) (repealed) (Supp. 1987). It is possible, though unlikely because of the interest of management of corporations that were, or were potential, targets

Combination Act was challenged in one attempted takeover of an Indiana corporation, but the issue was mooted when the proposed acquisition was held to violate the federal antitrust law.⁶⁴

The challenge to the Control Share Acquisition Chapter of the IBCL, on the other hand, went all the way to the United States Supreme Court in *CTS Corp. v. Dynamics Corporations of America*.⁶⁵ Dynamics Corporations of America's (DCA) attempt to obtain control of CTS was a prolific generator of legal issues and judicial decisions: one in the Indiana Court of Appeals,⁶⁶ three in the United States District Court for the Northern District of Illinois,⁶⁷ one in the Seventh Circuit Court of Appeals,⁶⁸ and one in the United States Supreme Court.⁶⁹ The Supreme Court's decision resulted in three separate opinions.⁷⁰

The most important of the lower court opinions was Judge Posner's opinion in the Seventh Circuit⁷¹ holding that the Control Share Acquisition provisions of the IBCL violated both the supremacy and commerce clauses of the United States Constitution.⁷² Judge Posner first discussed

of hostile takeover attempts, that corporations might not have learned of Senate Bill No. 1 until after the opt out period had elapsed.

⁶⁴Laidlaw v. Mayflower Group, 636 F. Supp. 1513 (S.D. Ind. 1986).

⁶⁵107 S.Ct. 1637 (1987).

⁶⁶Dynamics Corp. of America v. CTS Corp., 479 N.E.2d 1352 (Ind. Ct. App. 1985).

⁶⁷Dynamics Corp. of America v. CTS Corp., 637 F. Supp. 406 (N.D. Ill. 1986); Dynamics Corp. of America v. CTS Corp., 635 F. Supp. 1174 (N.D. Ill. 1986); Dynamics Corp. of America v. CTS Corp., Fed. Sec. L. Rep. (CCH) ¶ 92,765 (N.D. Ill. May 3, 1986).

⁶⁸Dynamics Corp. of America v. CTS Corp., 794 F.2d 250 (7th Cir. 1986).

⁶⁹107 S.Ct. 1637 (1987).

⁷⁰Justice Powell delivered the opinion of the Court, in which Chief Justice Rehnquist, and Justices Brennan, Marshall, and O'Connor joined. Justice Scalia joined in Parts I, III-A, and III-B, of the majority's opinion and filed an opinion concurring in part and concurring in the judgment. Justice White filed a dissenting opinion, in Part II of which Justices Blackmun and Stevens joined.

⁷¹794 F.2d 250 (7th Cir. 1986).

⁷²Judge Posner also affirmed the decision in *Dynamics Corp. of America v. CTS Corp.*, 637 F. Supp. 406 (N.D. Ill. 1986) enjoining CTS's management from enforcing a "poison pill" plan adopted by CTS during a proxy contest between management and DCA. DCA sought injunctive relief under section 14(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78n(a) (1982), alleging an unlawful proxy solicitation by CTS management, 637 F. Supp. at 407.

Judge Posner was not impressed with the poison pill as a plausible measure for maximizing shareholder wealth. He conceded that it was not certain CTS shareholders, other than DCA, would be worse off if the pill was triggered, but he felt it was too high a price to pay for preventing a shift in control from incumbent CTS management to DCA. DCA could not have squeezed out remaining shareholders because it would not own a majority of shares even if the tender offer succeeded. A *reasonable* defensive move would have been a device that would be triggered by a transaction creating a majority shareholder or an attempt to squeeze out minority shareholders in an unfair transaction.

the supremacy clause issue: was the Control Share Acquisition chapter preempted by the Williams Act?⁷³ He characterized the statute as “cleverly drafted . . . to skirt judicial holdings that forbid states to delay tender offers beyond the period required by the Williams Act.”⁷⁴ The effect of the statute as he perceived it was to impose a fifty day delay on tender offers at the option of the target. This made it more difficult for any tender offer to succeed because an offeror could not accept tendered shares until the shareholder meeting where it will be determined if the shares will carry voting rights. Thus a tender offer would have to be kept open for fifty days rather than the twenty business days required by SEC Rule 14e-1(a),⁷⁵ and even then the offeror cannot be certain of a victory because the “disinterested” shareholders must approve the vote.⁷⁶

Judge Posner reasoned that even though the *MITE* Court did not accept the preemption argument, it held that Congress intended to strike a balance between target management and offerors in the Williams Act.⁷⁷ From this premise courts have reasoned that states may not upset the balance struck by Congress.⁷⁸ To Judge Posner, the Williams Act does exist and it does strike a balance.⁷⁹ Regardless of whether the balance is proper or desirable as an economic matter, Congress probably did not want the states to tip the “balanced playing field” one way or the other. The Indiana statute might be less offensive than the statute in *MITE*, but the fifty day period was still “too much.”⁸⁰

Even if the Control Share Acquisition Chapter could survive a preemption challenge, Judge Posner made it clear that it would still fall under the commerce clause. The commerce clause invalidates state regulation of interstate commerce that conflicts with the presumed purpose

794 F.2d 250, 254-59.

Judge Posner drolly turned one CTS argument against itself: If a DCA controlled board of directors of CTS could “gull” the remaining shareholders, then corporate management cannot be trusted to protect the interest of shareholders. 794 F.2d at 259.

⁷³15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1982).

⁷⁴794 F.2d at 261.

⁷⁵SEC Rule 14e-1(a); 17 C.F.R. § 240.14e-1(a) (1986).

⁷⁶794 F.2d at 261. One possible unforeseen consequence of a statute like the Control Share Acquisition Chapter is that it might tempt offerors to put an offer into play where management owns a substantial number of shares knowing that management will be disenfranchised. In fact a Minnesota corporation was forced into the arms of a white knight for this reason after Minnesota adopted at the behest of the Dayton-Hudson Corporation, an antitakeover statute similar to the Control Share Acquisition Chapter.

⁷⁷794 F.2d at 262. See *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1 (1977).

⁷⁸See, e.g., *Martin-Marietta Corp. v. Bendix Corp.*, 690 F.2d 558, 567-68 (6th Cir. 1982); *National City Lines, Inc. v. LLC Corp.*, 687 F.2d 1122, 1128-33 (8th Cir. 1982).

⁷⁹*Dynamics Corp.*, 794 F.2d at 262.

⁸⁰*Id.*

of the clause to make the nation a common market, at least where Congress has not spoken.⁸¹ *MITE* and other cases separate the supremacy and the commerce clauses and assume that the commerce clause retains an independent force notwithstanding the enactment of the Williams Act.⁸² In this respect, Judge Posner, in *Dynamics*, stated there was no indication the Williams Act was intended to insulate antitakeover statutes from complaints that they unduly burden interstate commerce.⁸³

The commerce clause does not bar all state action that might impose some burden on interstate commerce. Statutes will be upheld if local benefits exceed the burden imposed in interstate commerce.⁸⁴ Applying this test, Judge Posner concluded the burdens the Control Share Acquisition Chapter inflicted on nonresidents exceeded the benefits to Indiana residents. He assumed that the vast majority of DCA or CTS shareholders were not Indiana residents. Consequently the statute gravely impaired DCA's ability to do business with those shareholders. Or as he phrased it, "Indiana has no interest in protecting residents of Connecticut from being stampeded to tender their shares to Dynamics at \$43."⁸⁵ He also stated, "For the sake of trivial or even negative benefits to its residents Indiana is depriving nonresidents of the valued opportunity to accept tender offers from other nonresidents."⁸⁶ He even doubted if any appreciable number of Indiana shareholders would benefit from the statute and stated that the only beneficiaries might be the officers and directors of CTS.⁸⁷ In essence Indiana was attempting to opt out of the interstate and international market for corporate control, an effort barred by the commerce clause.

The Seventh Circuit rejected CTS's argument that Indiana should be permitted to control the "internal affairs" of Indiana corporations.⁸⁸ Judge Posner, of course, recognized that Indiana has broad latitude in regulating internal affairs of Indiana corporations. This includes the right to authorize provisions in corporate documents that discourage takeovers.⁸⁹ However, he concluded there are limits to the internal affairs

⁸¹*Id.* at 263. See *Cooley v. Board of Wardens*, 53 U.S. 249 (1852).

⁸²*Dynamics Corp.*, 794 F.2d at 263. See *Edgar v. MITE Corp.*, 457 U.S. 657 (1982).

⁸³*Dynamics Corp.*, 794 F.2d at 263.

⁸⁴See *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970). A majority of the Court in *MITE* found that the Illinois statute violated the commerce clause as an undue, indirect burden on interstate commerce. *Edgar v. MITE Corp.*, 457 U.S. 624, 640-46 (1982).

⁸⁵*Dynamics Corp.*, 794 F.2d at 263.

⁸⁶*Id.* at 264.

⁸⁷*Id.*

⁸⁸*Id.*

⁸⁹*Id.* The court referred to cumulative voting, which can make it difficult to oust an entire existing board of directors. A staggered board of directors would also be permitted even though it was a defensive move by management. *Id.*

doctrine, which are exceeded when the state regulation has an effect “on the interstate market in securities and corporate control [that] is direct, intended and substantial . . . [and] not merely the incidental effect of a general regulation of internal corporate governance.”⁹⁰ As Judge Posner accurately, if not elegantly, phrased it, the Control Share Acquisition Chapter is an explicit regulation of tender offers and is not immunized from the commerce clause because “the mode of regulation involves jiggering with voting rights. . . .”⁹¹ It was primarily on the “internal affairs doctrine” that the Supreme Court reversed the Seventh Circuit.⁹² The Court, of course, discussed both grounds relied on by the lower courts in striking down the Indiana statute. Justice Powell, writing for the majority, first discussed the Williams Act preemption issue, and concluded that because it is entirely possible for entities to comply with both the Williams Act and the Indiana Act, the state statute can be preempted only if it frustrates the purposes of the federal law.⁹³

It is interesting that the majority did not reject the preemption test outright. Rather it assumed that such a test might be appropriate but that the Control Share Acquisition Chapter passed muster because it did not tilt unduly the playing field towards target management. It just gave “shareholders the power to deliberate collectively about the merits of tender offers.”⁹⁴ The Court examined the delay inherent in consummating tender offers until after the shareholder vote; discussed and seemingly authorized contingent tender offers;⁹⁵ and expressed concern that invalidating the Control Share Acquisition Chapter on a preemption ground would cast doubt on the validity of other aspects of state corporate law that might delay a control transaction.⁹⁶ The Court noted that “[t]he desire of the Indiana Legislature to protect shareholders of Indiana corporations from this type of coercive offer does not conflict with the Williams Act. Rather, it furthers the federal policy of investor protection.”⁹⁷

⁹⁰*Id.*

⁹¹*Id.*

⁹²*CTS Corp. v. Dynamics Corp. of America*, 107 S.Ct. 1637, 1646-52 (1987).

⁹³*Id.* at 1644-48, *citing* *Ray v. Atlantic Richfield Co.*, 435 U.S. 151, 158 (1978).

⁹⁴*CTS*, 107 S.Ct. at 1646 n.7.

⁹⁵*Id.* at 1647 n.8.

⁹⁶*Id.* at 1647. However, it really does not follow automatically that invalidating state antitakeover legislation would invalidate traditional corporate law concepts such as staggered boards and cumulative voting. After all, as Judge Posner pointed out, the Control Share Acquisition Chapter was intended to delay and hinder takeovers whereas provisions such as cumulative voting and staggered boards serve other purposes, and have for many years, even though they may delay an offeror from getting immediate control of a board of directors. The delay would be “merely the incidental effect of a general regulation of internal corporate governance.” *Dynamics Corp.*, 794 F.2d at 264.

⁹⁷*CTS*, 107 S.Ct. at 1646.

This might be true, but Justice Powell's opinion does not reflect the fact, as reported in *The Wall Street Journal*, that the Chairman of Arvin Industries had asked the President of the Indiana Senate to:

"help stop . . . [a threatened] takeover and save Arvin Industries and Columbus from wrenching change, [and that the President of the Senate] didn't let him down. Within four weeks, he had steered a tough anti-takeover bill, drafted by Arvin's own lawyers, through the Indiana Legislature and onto the governor's desk, where it was promptly signed. The bill, in effect, outlawed most hostile takeovers in the Hoosier State."⁹⁸

One scholar has observed that Williams Act preemption scrutiny of various types of state regulation is still possible after *CTS*, but that "[w]hether the preemption bar will come down on statutes equally voluntary but authorizing a different constraint such as a 'fair price put' for remaining shareholders, or substantively like Indiana's but mandatory, is not clear."⁹⁹ It is possible, but perhaps unlikely considering the "tone" of the majority opinion. The majority did not flatly reject preemption in the takeover area, but certainly the opinion cannot be called sympathetic to preemption, short of instances where compliance with the Williams Act and state antitakeover statutes "is a physical impossibility."¹⁰⁰

The majority's resolution of the commerce clause issue in *CTS* started from the premise that "[t]he principal objects of dormant Commerce Clause scrutiny are statutes that discriminate against interstate commerce."¹⁰¹ The Control Share Acquisition Chapter was deemed "non-discriminatory" because it applies to offerors whether or not domiciliaries or residents of Indiana. It rejected Dynamics' argument that it was discriminatory because most hostile tender offers will be launched by non-Indiana offerors: "[b]ecause nothing in the Indiana Act imposes a

⁹⁸Wall St. J., July 1, 1987, at 1, col.6. This was Senate Bill No. 1. The same article quoted an official at the Columbus Chamber of Commerce that the focus of an out-of-town owner "is on the bottom line and the return to shareholders." *Id.* p.14, col. 1. So much for protection of investors. It really is a legitimate question to ask just whose interests are being protected by antitakeover statutes such as the Control Share Acquisition Chapter. The statute might be couched in terms of shareholder action, but shareholders do not seem to have been the primary beneficiaries of Senate Bill No. 1.

⁹⁹Buxbaum, *The Threatened Constitutionalization of the Internal Affairs Doctrine in Corporation Law*, 75 CALIF. L. REV. 29, 31 (1987).

¹⁰⁰*CTS*, 107 S.Ct. at 1644.

¹⁰¹*CTS*, 107 S.Ct. at 1648. See, e.g., *Lewis v. BT Invest. Managers, Inc.*, 447 U.S. 27, 36-37 (1980); *Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978). See generally Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 MICH. L. REV. 1091 (1986).

greater burden on out-of-state offerors than it does on similarly situated Indiana offerors, we reject the contention that the Act discriminates against interstate commerce.”¹⁰²

One criticism of decisions such as Judge Posner’s is that they tend to raise the “free market” school to a constitutional status. However, the Court’s analysis of the commerce clause can be criticized because it comes “dangerously close to embedding another doctrine—the ‘state of incorporation’ version of the internal affairs doctrine—in the Constitution via the same clause.”¹⁰³

Justice Powell concluded that the Seventh Circuit’s holding that the Control Share Acquisition Chapter was invalid because it hinders tender offers ignored the fact that states as overseers of corporate governance, enact laws that necessarily affect certain aspects of interstate commerce, particularly with respect to corporations with shareholders in other states.¹⁰⁴ He notes that “[a] state has an interest in promoting stable relationships among parties involved in the corporations it charters, as well as in ensuring that investors have an effective voice in corporate affairs.”¹⁰⁵ The Indiana statute, accordingly, validly furthered these interests by allowing shareholders collectively to determine whether a takeover is advantageous to them. Justice Powell rejected the argument that Indiana has no legitimate interest in protecting nonresident shareholders because the Control Share Acquisition Chapter applies only to corporations incorporated in Indiana that have a substantial number of shareholders in the state.¹⁰⁶

¹⁰²*CTS*, 107 S.Ct. at 1649. Of course this is something like saying that the law does not discriminate against the poor because the law in all its majesty prohibits both the rich and the poor from sleeping under bridges.

¹⁰³Buxbaum, *supra* note 99, at 34-35. Professor Buxbaum did deem it laudable that the Court used the internal affairs doctrine to avoid raising efficient-capital and control-market hypotheses to the level of constitutional doctrine via the dormant commerce clause, as *MITE* and Judge Posner seemed to be doing. *Id.* at 34.

¹⁰⁴*CTS*, 107 S.Ct. at 1649-50. For example mergers may require super-majority approval or dissenting shareholders may have appraisal rights.

¹⁰⁵107 S.Ct. at 1651.

¹⁰⁶*Id.* 107 S.Ct. at 1651-52. The Control Share Acquisition Chapter applies to publicly held corporations that have:

- (1) one hundred (100) or more shareholders;
- (2) its principal place of business, its principal office, or substantial assets within Indiana; and
- (3) either:
 - (A) more than ten percent (10%) of its shareholders resident in Indiana;
 - (B) more than ten percent (10%) of its shares owned by Indiana residents; or;
 - (C) ten thousand (10,000) shareholders resident in Indiana.

IND. CODE § 23-1-42-4(a) (Supp. 1987).

There is something deliciously ironic in characterizing the Control Share Acquisition Chapter of the IBCL as being protective of the interests of shareholders of Indiana corporations. Most modern "flexible" corporation statutes have cut back the role and rights of shareholders in favor of management control of corporate affairs. This observation is particularly true with respect to the IBCL when the provisions of the Indiana statute are compared with the provisions of the Revised Model Business Corporation Act on which it is based.¹⁰⁷

The Court in *CTS* refused to take sides in the debate over the merits or demerits of tender offers.¹⁰⁸ Rather it deferred to the empirical judgment of lawmakers.¹⁰⁹ This is a rather clear rejection of the "free market" approach to corporate regulation.¹¹⁰ Perhaps there would be something wrong with a "federal regime that relies solely on 'the market' to regulate these structural phenomena [which] is cold comfort to local political units called upon to bear the costs of economic change today while the greater benefits of tomorrow manifest themselves elsewhere."¹¹¹ Of course, one might wonder just how sincere states and local political units are about "preserving" corporate presence and rank and file jobs. It is not unusual to pick up *The Wall Street Journal* to read about states adopting an antitakeover statute similar to Indiana's and also read about state efforts to woo businesses to relocate within their borders by means of tax abatements, other subsidies, a nonunion work force or even low worker's compensation costs. Few states, not including Indiana, can boast they do not engage in the game of "beggar thy neighbor."¹¹²

Justice Scalia joined with the majority on the commerce clause issue.¹¹³ In fact his concurring opinion will bring pleasure to those openly

¹⁰⁷See 1-4 Model Bus. Corp. Act Ann. (3d ed. 1985).

¹⁰⁸*CTS*, 107 S.Ct. at 1651-52 and n.12.

¹⁰⁹*Id.* at 1651.

¹¹⁰See generally Easterbrook & Fishel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981).

¹¹¹Buxbaum, *supra* note 99, at 32. See generally Stewart, *Pyramids of Sacrifice? Problems of Federalism in Mandating State Implementation of National Environmental Policy*, 86 YALE L. J. 1196 (1977).

¹¹²The *CTS* majority did not resolve *CTS*'s argument that the Control Share Acquisition Chapter "does not violate the Commerce Clause—regardless of any burdens it may impose" on interstate commerce—because a corporation's decision to be covered by the Act is purely 'private' activity beyond the reach of the Commerce Clause" 107 S.Ct. at 1652 n.14. This "contractarian" distinction might become more important or at least in issue, if, as is likely, states are pressured for still more vigorous antitakeover devices than are permitted by *CTS*. See Buxbaum, *supra* note 99, at 56. Of course, the question may very well be mooted if the number of hostile tender offers decrease because of the stock market crash of 1987.

¹¹³*CTS*, 107 S.Ct. at 1652-53 (Scalia, J., concurring).

favoring management in the takeover game since he says, "Nothing in the Constitution says that the protection of entrenched management is any less important a 'putative local benefit' than the protection of entrenched shareholders. . . ." ¹¹⁴ Justice Scalia can be commended in apparently recognizing that statutes such as the Indiana Control Share Acquisition Chapter are the result of pressure from managements threatened by hostile takeovers: Arvin in Indiana; Gillette Company in Massachusetts; Ashland Oil in Kentucky; Dayton-Hudson in Minnesota; Burlington Industries in North Carolina. ¹¹⁵ It is very telling that as the state of incorporation of a target, Delaware—a state which is as likely to be the state of incorporation of an offeror—has not followed Indiana's lead and, at least at present, has decided against a law curbing takeovers. ¹¹⁶ The refusal of the state with the most to lose if corporations flee to Indiana, or other states with similar or stronger antitakeover statutes, to adopt an antitakeover statute says something about the wisdom of antitakeover devices that are mandated by statute rather than adopted by shareholder actions. ¹¹⁷ As one observer has noted:

[G]iven the ready availability of self-help what need is there for a statute? While a statute certainly saves the cost of a shareholder vote for firms that would otherwise voluntarily adopt such a provision, one cannot help but suspect that managers gripped by fear of losing their jobs lobby for legislation because they worry that a majority of their firm's shareholders would not approve a charter amendment. ¹¹⁸

Of course, it was Justice Scalia who said that a "law can be both economic folly and constitutional." ¹¹⁹

Justice Scalia departed from the majority on the Williams Act preemption issue, although he too agreed the Control Share Acquisition Chapter was not preempted. Rather than debating the purposes of the

¹¹⁴*Id.* at 1653.

¹¹⁵See Goodman, *State Takeover Legislation*, 1 INSIGHTS No. 3 at 2 (Sept. 1987). See also *State vs. Raiders: Will Washington Step In?*, BUS. WK. (August 31, 1987) at 56.

¹¹⁶Wall St. J., June 16, 1987, at 4, col. 4. See also Black, *Why Delaware is Wary of Anti-Takeover Law*, Wall St. J., July 10, 1987, at 16, col. 3. Mr. Black in his editorial piece raised the interesting point that the Control Share Acquisition Chapter provides a ready means of putting a company into play, certainly something not intended by the drafters of the statute.

¹¹⁷See Romano, *State Takeover Laws: Constitutional but Dumb*, Wall St. J., May 14, 1987, at 22, col. 4.

¹¹⁸*Id.* Shareholders may vote on whether to give voting rights to acquired control shares, but they vote on opting out of the statutory scheme only if management presents the decision to them. See IND. CODE § 23-1-42-5 (Supp. 1987).

¹¹⁹*CTS Corp. v. Dynamics of America*, 107 S.Ct. at 1654 (1987).

two statutes, Justice Scalia relied on section 28(a), the antipreemption provision of the Securities Exchange Act of 1934.¹²⁰

He recognized that section 28(a) did not literally apply to the Control Share Acquisition Chapter, but read it extremely broadly as applying to any corporate statute and not just state blue sky laws.¹²¹ Under Justice Scalia's approach preemption is foreclosed on the basis of a "conflicting purpose" and only applies when there is a "conflicting provision."¹²²

Justice White wrote a dissenting opinion in *CTS* asserting that the Indiana statute is both preempted by the Williams Act and conflicts with the commerce clause.¹²³ He maintained, as he did for the plurality in *MITE*,¹²⁴ that the purpose of the Williams Act was to ensure the individual investors are given sufficient information so they can make an informed choice on whether to tender their shares in response to a tender offer. The problem he saw with the approach of the *CTS* majority was that it equates protection of individual investors, the focus of the Williams Act, with the protection of shareholders as a group.¹²⁵ The statute might help protect the interests of a majority of the shareholders in any corporation but in many instances it could effectively prevent an individual investor from selling his or her stock at a premium.¹²⁶ Consequently, it does not "furthe[r] the federal policy of investor protection," and so should fall under the supremacy clause.

One particularly telling point raised by Justice White is that the Control Share Acquisition Chapter is not simply a regulation of "shareholder voting rights" as characterized by proponents of the statute. Rather it is *transactional* in nature designed to thwart certain takeovers.¹²⁷ If this distinction is kept in mind, then the perceived threat preemption poses to other corporate control provisions such as cumulative voting and staggered boards is nothing more than a red herring.

On the commerce clause issue, Justice White concluded that the Court should not countenance a statute that effectively precludes a prospective purchaser from purchasing a target's shares "if the purchaser

¹²⁰15 U.S.C. § 78bb(a) (1982). This section provides that nothing the 1934 Act contains "shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this chapter or the rules and regulations thereunder." *Id.*

¹²¹*CTS*, 107 S.Ct. at 1653 (Scalia, J., concurring).

¹²²*Id.*

¹²³*Id.* at 1653-56 (White, J., dissenting). Justices Blackmun and Stevens joined the dissent on the commerce clause issue.

¹²⁴*Edgar v. MITE Corp.*, 457 U.S. 624 (1982).

¹²⁵*CTS*, 107 S.Ct. at 1654.

¹²⁶*Id.*

¹²⁷*Id.* at 1655.

crosses one of the Chapter's threshold ownership levels and a majority of . . . [the target's] shareholders refuse to give the purchaser voting rights"¹²⁸ because it is a restraint on interstate trade. Furthermore, he characterized a state law which permits a majority of a corporation's shareholders to prevent individual investors, including non-residents, from selling their shares to an out-of-state tender offeror and thereby frustrate any transfer of corporate control, as "the archetype of the kind of state law that the commerce clause forbids."¹²⁹

The dissenting Justices obviously were more concerned with the blocking of interstate transactions in securities than was the majority. They realized that the goal of the commerce clause was to prevent "economic Balkanization."¹³⁰ There is no question but that the statute upheld in *CTS* presents such a risk, although it is not a foregone conclusion. It is highly unlikely that many corporations will flee Delaware, with its long corporate law history and a corporation statute that permits corporations to shield directors from liability,¹³¹ to Indiana simply to get the protection of the Control Share Acquisition Chapter. Furthermore, few large publicly held corporations could do this because they are not "Indiana businesses." Some true "Indiana businesses" incorporated in Delaware have reincorporated in Indiana, and others might do the same, unless Delaware decides to adopt an antitakeover statute. What will likely happen is that more and more states will adopt antitakeover statutes. If they simply follow Indiana there will not be a problem, other than the problems that might result from the demise of the takeover game. However, if the statutes are tailored to meet the needs of a particular local corporation, and there is too much variance, the end result might be federal legislation clearly preempting the field of takeover regulation. Efforts to this effect already have started in Congress.¹³²

¹²⁸*Id.*

¹²⁹*Id.*

¹³⁰*Id.* at 1655, quoting from *Hughes v. Oklahoma*, 441 U.S. 322, 325-26 (1979).

¹³¹DEL. CODE ANN. tit. 8 § 102(b)(7) (Supp. 1986).

¹³²See letter from Rep. Norman F. Lent (R. N.Y.), *Wall St. J.*, Sept. 21, 1987, at 23, col. 1.

Of course amending the Williams Act to make takeover law uniform throughout the country, and to solve any real, or imagined problems with the current takeover scene will not satisfy all critics of hostile takeovers. See Grippio, *MITE Made Right: The Supreme Court Gives Illinois New Hope for a Takeover Law*, ILL. B.J. 844 (Nov. 1987).

Critics who go beyond opposing hostile takeovers simply to help the "hometown boys" might have a point. SEC Chairman Ruder has announced the SEC plans to examine the role takeover stocks played in the October 1987 stock market crash. *The Wall St. J.*, Nov. 16, 1987, at 6, col. 1. In his speech Mr. Ruder reiterated the SEC position "that federal law should preempt state law in the area of tender offers . . . [and said that he believes] that corporations whose activities and ownership are national in scope shouldn't be given protection against takeovers by states where their primary production facilities are located." *Id.*

Only time will tell if this will happen, but it would be ironic indeed.

The reaction to *CTS* was predictable. Management generally applauded the decision¹³³ as did politicians.¹³⁴ Raiders did not,¹³⁵ nor did institutional investors,¹³⁶ many academics¹³⁷ and editorial writers.¹³⁸

With the constitutionality of second generation antitakeover statutes established in *CTS*, an interesting question is just how far states will go beyond the Indiana scheme in efforts to protect local companies. This would create the "Balkanization" feared by the dissenting Justices. Many states will adopt statutes modeled on the Indiana act, which applies only to domestic corporations; however, some will be tempted to try to control takeovers of foreign corporations with significant local interests.¹³⁹ Such efforts seem to run afoul of *CTS* which emphasized the state of incorporation, but it is possible that under some circumstances "local interests" of a foreign corporation may give a state precedence over the state of incorporation.¹⁴⁰ Only time will tell if such efforts will pass muster.

Probably an even more interesting question will be the success of "work arounds" the Control Share Acquisition Chapter. It must be remembered that the *CTS* majority in effect embraced Williams Act supremacy clause preemption although it found it inapplicable in the particular case. This can be contrasted with *MITE* where the position was rebuffed by the Court. Only Justice Scalia's concurring opinion categorically rejected preemption short of "conflicting provisions" in state and federal regulatory schemes.¹⁴¹ The Court at least implicitly recognized contingent tender offers, which are offers to accept shares on the condition the shares receive voting rights within a certain period

¹³³See *Takeover Artists Take a Direct Hit*, BUS. WK., May 4, 1987, at 35.

¹³⁴See, e.g., Bayh, *The CTS Case*, 4 INDIANA SECURITIES BULLETIN 1 (April 1987).

¹³⁵See *Takeover Artists Take a Direct Hit*, BUS. WK., May 4, 1987 at 35.

¹³⁶Wall St. J., April 24, 1987, at 4, col. 2.

¹³⁷See Romano, *State Takeover Laws: Constitutional but Dumb*, Wall St. J., May 14, 1987, at 22, col. 4.

¹³⁸Wall St. J., April 23, 1987, at 26, col. 1. Following the decision in *CTS* even the Indianapolis Business Journal observed that "[a]s it stands now, the state of Indiana and the managers and employees of its public companies are winners. The large number of investors may, in fact, be losers." Indianapolis Bus. J., April 27-May 3, 1987, at 6, col. 1.

¹³⁹See Comment, *Beyond CTS: A Limited Defense of State Tender Offer Disclosure Requirements*, 54 U. CHI. L. REV. 657, 658 (1987).

¹⁴⁰See Buxbaum, *supra* note 99, at 54. Professor Buxbaum posits that in the case of a Delaware corporation with all shareholders residing in California and none in Delaware a "Court faced with an absolute dilemma (e.g., inconsistent rules) may well give primacy to the shareholder state." *Id.*

¹⁴¹*CTS*, 107 S.Ct. at 1653 (Scalia, J., dissenting).

of time.¹⁴² Thus a preemption problem might arise if states attempt to foreclose such contingent offers. Such efforts might be tempting if the contingent offer "work around" puts management on the spot; however, such provisions may tilt the playing field too much in management's favor even in the eyes of the *CTS* majority.

Corporate management of Indiana already have a decided advantage over offerors when it comes to voting on control share acquisition resolutions. At least management that has had the foresight to establish an employee benefit plan that owns shares of the corporation possess the advantage.

Common law¹⁴³ and statutes¹⁴⁴ generally prohibit voting of shares of a corporation owned, directly or indirectly, by a second corporation, either domestic or foreign, where the corporation owns, directly or indirectly, a majority of shares entitled to vote for directors of the second corporation. This restriction on circular ownership is designed to prevent management from perpetuating control by the corporation's direct or indirect ownership of its own shares. Such shares may be voted in "special circumstances"¹⁴⁵ which means where the purpose of the provision is not violated.¹⁴⁶

There was some question at common law whether a corporation could vote its own shares held in a fiduciary capacity. Section 23-1-30-2(c) of the IBCL provides that the bar against circular voting does not limit the power of a corporation to vote shares "held by it in or for an employee benefit plan or in any other fiduciary capacity."¹⁴⁷ Voting shares held in an employee benefit plan on a control share acquisition resolution against an offeror could, and maybe should, be characterized as an effort by management to use a corporate investment to perpetuate itself in power. However, the definition of "interested shares" in the Control Share Acquisition Chapter is very specific. It refers to shares an officer or employee director of an issuing corporation "may exercise or direct the exercise of the voting power of the corporation in the election of directors."¹⁴⁸ The vote of shares held in an employee benefit plan would be a corporate act, and not the act of the officers or

¹⁴²*Id.* at 1647.

¹⁴³*See* 1 G. HORNSTEIN, CORPORATE LAW AND PRACTICE § 311 (1959).

¹⁴⁴*See, e.g.*, IND. CODE § 23-1-30-2(b) (Supp. 1987).

¹⁴⁵*Id.*

¹⁴⁶*See* 2 MODEL BUS. CORP. ACT ANN. § 7.21 official comment § 3 (3d. ed. 1985).

¹⁴⁷IND. CODE § 23-1-30-2(c) (Supp. 1987). The reference to "shares . . . held by it in or for an employee benefit plan" is not found in the comparable provision of the REVISED MODEL BUSINESS CORPORATION ACT, 2 Model Bus. Corp. Act Ann. § 7.21(c) (3d ed. 1985).

¹⁴⁸IND. CODE §§ 23-1-42-3(2), (3) (Supp. 1987).

directors. Consequently, they probably can be voted against an offeror. Management will argue that they are voting the shares to protect the interests of the employees just as they argue that opposing hostile tender offers are to protect the interests of shareholders.

It is possible that management efforts to defeat takeover attempts by devices that reduce the value of corporate shares, such as poison pills, asset options, etc., may result in director liability for breach of duty to shareholders. This point was raised by the Court in *CTS*.¹⁴⁹ Some cases support this result,¹⁵⁰ but as states adopt or amend corporation statutes limiting or even eliminating director liability for breach of duty there is less likelihood that this will be a viable alternative.

As noted above,¹⁵¹ a possible result of *CTS* will be the enactment of new federal legislation regulating takeovers that will clearly preempt the field. Congress may decide that the problems with takeovers are national rather than statewide. The debate then will be, and properly should be, over the real or imagined faults in the current system. The result might be legislation deferring to the states, where threatened targets may be able to influence state legislatures. Alternatively, it might be a complete acceptance of the "free market" approach at least as reflected in the Seventh Circuit's decision in *CTS*.¹⁵² Or it may be somewhere in between. Again, only time will tell.

There are many questions that the *CTS* decision does not answer. For example, why are takeover attempts for corporations with less than 100 shareholders excluded from the typical state antitakeover statute? States should be as interested in protecting the shareholders of closely held or publicly held corporations with relatively few shareholders as they are in protecting the interests of shareholders of large publicly held corporations subject to Williams Act regulation. At least the latter have some market for their shares in case of mismanagement by those in control. There are many more small corporations than large with a greater likelihood that minority shareholders of closely held corporations will be frozen out by majority shareholders than there will be instances of shareholders of publicly held Indiana corporations being frozen out by a successful hostile offeror. These shareholders have little specific

¹⁴⁹*CTS Corp. v. Dynamics Corp. of America*, 107 S.Ct. at 1647, n.9. See also Buxbaum, *supra* note 99, at 57 n.88.

¹⁵⁰See *Hanson Trust PLC v. ML SCM Acquisition Inc.*, 781 F.2d 264 (2d Cir. 1986); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986).

¹⁵¹See *supra* note 132 and accompanying text.

¹⁵²*Dynamics Corp. of America v. CTS Corp.*, 794 F.2d 250 (7th Cir. 1986). See Grundfest, *Proxmire's Doubletalk on Takeovers*, Wall St. J., Sept. 16, 1987 at 30, col. 3; Sprinkel, *The Real Issue in Corporate Takeovers*, Wall St. J., July 17, 1987, at 14, col. 3.

statutory protection under corporation acts like the IBCL. Also, why are there no limits on self-tenders by corporations that can be harmful to shareholders?

Even more interesting, at least to this author, is the role of corporate "constituencies" other than shareholders. The IBCL clearly permits directors to consider such constituencies in making corporate decisions.¹⁵³ This would include decisions opposing hostile tender offers. However, directors are not required to do so and there is nothing in Indiana law that limits an Indiana corporation from simply moving plants and production facilities from the state. A Maine statute requiring employers to provide a one-time severance pay to employees in event of a plant closing recently was upheld by the Supreme Court.¹⁵⁴ Perhaps Indiana political leaders and the General Assembly, which was willing to adopt legislation that directly or indirectly protects the jobs of top management of Indiana corporations, should consider such a statute to protect the rank and file employee if management decides to move jobs out of state. Such a statute probably would not be well received by most proponents of state antitakeover laws.¹⁵⁵

¹⁵³See Grundfest, *Proxmire's Doubletalk on Takeovers*, Wall St. J., Sept. 16, 1987, at 30, col. 3; Sprinkel, *The Real Issue in Corporate Takeovers*, Wall St. J., July 17, 1987, at 14, col. 3.

¹⁵⁴*Fort Halifax Packing Co. v. Coyne*, 107 S.Ct. 2211 (1987).

¹⁵⁵There might be agreement on this point with opponents of state antitakeover statutes who favor the free market approach to corporate control.

A clearly unforeseen consequence of the Control Share Acquisition Chapter is that certain Indiana Corporations cannot sell their shares in California because it "negate[s] the democracy within the corporation by discriminating against a set of shareholders. Indianapolis Bus. J., December 21-27, 1987, at 3, col. 3.

