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ANDREW J. OPIOLA*

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INTRODUCTION

In response to worries about the coercive tactics of hostile bidders in corporate takeovers—particularly front-end loaded, two-tier tender offers—states began to enact antitakeover legislation in the 1980s to ensure a fair outcome between bidders and holdout shareholders.¹ The idea behind the front-end loaded, two-tier tender offer is simple.² By offering a higher price for, say, fifty-one percent of a target’s shares in the first step of a tender offer, and a lower price for the remaining shares if control is established during the first step, a bidder can presumably induce more shareholders to tender their shares than would have been possible in a single-tier tender offer.³ Partial offers may have a similar coercive effect because target shareholders may fear that the acquirer will loot the company. Coercion may therefore lead to the target corporation’s sale at too low a price. As a result, the long-term business plans of incumbent management may be threatened by a hostile bidder, thereby reducing the incentive to innovate. Nevertheless, courts and regulators have been reluctant to prohibit partial and two-tier tender offers because of the perceived benefits to shareholders.⁴

Control share statutes are one of several types of state takeover laws designed to reduce coercion.⁵ The Indiana Control Share Acquisitions Act ("Indiana Act"),⁶ which the Supreme Court upheld in CTS Corp. v. Dynamics Corp. of America,⁷ has been widely used as a model by other states adopting control share statutes. As of

* Associate, Blades & Rosenfeld, P.A.

2. Id. at 1640.
3. Id.
4. Id. at 1643. See also Perlman v. Feldman, 219 F.2d 173, 176–77 (2d. Cir 1955) (holding that controlling shareholder is liable to minority shareholders for a sale of his controlling shares if he deprives the corporation of a possible gain).
5. See Booth, supra note 1, at 1672–78 (discussing other state takeover statutes such as fair price statutes, business combination statutes, disclosure statutes and appraisal statutes).
the year 2000, twenty-seven states had some form of control share statute. In essence, control share acquisition statutes, such as the Indiana Act, prohibit any person or group that acquires a specified percentage, e.g., twenty percent, of outstanding shares in a covered company from voting those shares unless a majority of disinterested shareholders vote to restore voting rights.

Control share statutes are designed to reduce coercion by protecting holdout shareholders in proposed tender offers and changes in corporate control. The statutes accomplish this goal by giving holdout shareholders an effective veto through the right to vote collectively on sales of control, thereby reducing opportunities for coercion and reducing private pre-offer purchases.

Control share statutes also reduce coercion by giving holdout shareholders, in effect, the ability to negotiate for better terms in the back end. For example, if a corporation does not opt out of the Indiana Act, then whenever a bidder in an unsolicited tender offer acquires more than twenty percent of the outstanding shares of a company, the bidder—either an inside manager or director, or an outside acquiring individual or group—will be unable to vote those shares until a majority of the remaining eighty percent of shareholders vote favorably to grant the bidder that right. In short, the shares the bidder acquires are “sterilized” until the bidder receives voting rights from the remaining holdout shareholders.

Further, control share statutes level the playing field by excluding the incumbent controlling shareholders from voting to reinfranchise control shares, leaving only the disinterested holdout shareholders to decide whether a transaction should go through. Control share statutes therefore act as a negotiating mechanism in front-end loaded, two-tier tender offers, where there exist the competing interests of management who seek to remain in control of the corporation and holdout shareholders who seek the highest premium for their shares. As a result, holdout share-

9. Booth, supra note 1, at 1678.
11. Booth, supra note 1, at 1681-82.
12. Id. at 1681, 1683.
13. Ind. Code § 23-1-42-5 (2003) (stating that a corporation may opt out by including a provision in the bylaws or articles of incorporation providing that the Indiana Act shall not apply, so long as such a provision is added before a control share acquisition occurs).
14. Ind. Code § 23-1-42-1 (2003). Disinterested shares (i.e., those persons who are allowed to vote to reinfranchise control shares) under the Indiana Act are shares held by anyone except those shares held by the acquiring person as a result of the control share acquisition, those held by any officer of the issuing public corporation, and those held by any employee of the issuing corporation who is also a director. See Ind. Code § 23-1-42-3 (2003).
15. Booth, supra note 1, at 1679.
16. See id.
17. Id. at 1684.
holders' votes become equally valuable to the bidder who wants the shareholders to tender their shares and to management, who likely want to remain in control of the corporation. By denying interested shareholders such as the bidder and incumbent management the right to vote to reinfranschise shares acquired in a control share transaction, disinterested holdout shareholders hold the ultimate power to decide whether a tender offer is in their best interest.

Finally, by requiring a shareholder vote on all sales of control, statutes such as the Indiana Act grant holdout shareholders the right to vote on whether inside sales of control ever go through. Such was the case in Perlman v. Feldmann, which coincidentally involved an Indiana corporation. A sale of control is essentially equivalent to a partial bid by an outsider. That is, an outside purchaser may be motivated to pay a premium for the controlling shares because he intends to loot the corporation or because the purchaser believes he can make the corporation more profitable and can buy the corporation at the lowest price by dealing only with the controlling shareholder. In either case, control share statutes give the holdout shareholders the right to vote on whether such sales should go through.

Today there are few front-end loaded, two-tier tender offers. Nevertheless, commentators continue to debate the inherent coercive nature of tender offers. Arguably, the use of such tactics has declined because of increased competition among bidders, the use of defensive tactics such as the poison pill by target corporations, and the effect of state takeover statutes. Thus, legal scholars have favored control share statutes in concept, but have also recognized that these statutes were by no means perfect as enacted. Indeed, it has been argued that these statutes may have resulted in numerous unforeseen consequences. A recent decision by the United States District Court for the Eastern District of Michigan in Simon Property Group, Inc. v. Taubman Centers, Inc. offers a prime example.

Taubman Centers Inc. (TCI) is a publicly traded real estate investment trust that conducts its regional shopping center operations through a limited partnership
NEWLY ISSUED SHARES & CONTROL SHARE STATUTES

known as Taubman Realty Group L.P. (TRG). TCI is the managing partner of TRG. In 1998 when it was learned that a limited partner was going to withdraw its investment in TRG, the board of directors of TCI authorized a new class of stock, called Series B Preferred Stock, to be issued to the limited partners of TCI, including the Taubman family. The move was arguably intended to simplify the ownership structure of the company, which it was thought had contributed to a low stock price. Before the new shares were issued, the Taubman family controlled a one-percent voting interest in TCI. Afterwards, the family gained a thirty-percent voting interest in TCI.

OPERATING INTERESTS IN TRG BEFORE AND AFTER ISSUANCE OF SERIES B PREFERRED STOCK

<table>
<thead>
<tr>
<th>Owners</th>
<th>Before</th>
<th>After</th>
</tr>
</thead>
<tbody>
<tr>
<td>GM</td>
<td>38%</td>
<td>—</td>
</tr>
<tr>
<td>TCI</td>
<td>39%</td>
<td>63%</td>
</tr>
<tr>
<td>Taubman Family</td>
<td>23%</td>
<td>37%</td>
</tr>
</tbody>
</table>

OWNERSHIP INTERESTS IN TCI BEFORE AND AFTER SERIES B PREFERRED STOCK WAS ISSUED

<table>
<thead>
<tr>
<th>Owners</th>
<th>Before</th>
<th>After</th>
</tr>
</thead>
<tbody>
<tr>
<td>Other Shareholders</td>
<td>79%</td>
<td>66.4%</td>
</tr>
<tr>
<td>GM</td>
<td>20%</td>
<td>—</td>
</tr>
<tr>
<td>Taubman Family</td>
<td>1%</td>
<td>30%</td>
</tr>
<tr>
<td>Taubman Family with Voting Agreements</td>
<td>—</td>
<td>33.6%</td>
</tr>
</tbody>
</table>

On November 13, 2002, Simon Property Group (SPG) publicly announced its offer to purchase all the outstanding stock of TCI. TCI issued a press release rejecting the offer on the same day. The following day, Robert Taubman “filed a Schedule 13D/A with the Securities and Exchange Commission (SEC) advising that he had entered into voting agreements with three, unrelated shareholders . . . for

27. TRG partnership interests are allocated as units. The Taubman family owned about 23% of these units and the General Motors (GM) pension trust, and TCI owned the remaining units. In 1998, GM decided to reduce its interest in TCI/TRG. Each limited partner in TRG received one share of Series B Preferred Stock for each TRG unit held. As a result, the Taubman family's voting power in TCI increased to 30% after the Series B Preferred Stock was issued.
28. In 1992, when TCI was taken public, 99% of the common stock was owned by public shareholders, including the GM pension trust that owned about 20% of the common stock of TCI. The limited partners each received one share of Series B stock for each TRG unit held, at $0.001 per share.
the purposes of preventing an unsolicited takeover of the company.”

The voting agreements combined with the Series B stock issued gave the Taubman family control of 33.6% of the voting stock of TCI and a blocking position over a sale of the corporation and the amendment or elimination of an excess share provision.

The Simon court faced three issues. First, did SPG have standing to bring a claim for breach of fiduciary duty based on the issuance of the Series B stock? Second, was the Series B stock issued by the TCI board to the Taubman family a control share acquisition under the Michigan Control Share Acquisition Act (“Michigan Act”)? Third, was the share acquisition that gave Robert Taubman and the Taubman family 33.6% voting power in TCI a group acquisition governed by the Michigan Act?

The question of what constitutes the formation of a group has been largely resolved by the state courts with guidance from the federal courts. Although neither the Michigan Act nor the Indiana Act defines the term group, the comments to the Indiana Act say the term group as used in section 13(d) of the Securities and Exchange Act offers clear guidance to state courts when determining the existence of

30. Id. “TCI’s Articles of Incorporation, via its ‘Excess Share Provision,’ prohibit anyone from acquiring shares in excess of 8.23% of the value of the outstanding capital stock of TCI (except certain persons who may own up to 9.9%).” Id. at 925. Further, “the provision can only be amended or eliminated by a two-thirds vote of TCI’s shareholders.” Id.
31. Id. at 932.
33. Simon, 240 F. Supp. 2d at 646.
34. 809 A.2d 1163 (Del. Ch. 2002).
37. Id. at 651. The court in a subsequent motion for a preliminary injunction held that “the Taubman family formed a group for the purpose of obtaining the practical ability to direct 33.6% of the voting power of TCI.” Simon, 261 F. Supp. 2d at 943, Mot. for Stay Pending Appeal granted, 262 F. Supp. 2d 794 (E.D. Mich. 2003). In September 2003, the Michigan Legislature passed Public Act 181 amending Mich. Comp. Laws § 450.1791, which provided that the “formation of a group does not constitute a control share acquisition” under the Michigan Act and added Mich. Comp. Laws § 450.1798a to ensure that the new law retroactively affected the Simon case directly. Glancy v. Taubman Centers, Inc., 373 F.3d 656, 661 n.5 (6th Cir. 2004).
a group under the Indiana Act.\textsuperscript{40} Moreover, the U.S. District Court for the Western District of Michigan in \textit{Atlantis Group Inc. v. Alizac Partners}\textsuperscript{41} cited and relied on the Indiana comments and section 13(d) to resolve the definition of a group under the Michigan Act.\textsuperscript{42}

The \textit{Simon} case raises two issues—whether forming a group of already existing shareholders to acquire a controlling interest above the statutory limit violates the Michigan Act and whether newly issued shares to controlling shareholders above the statutory limit violates the Michigan Act. But they are actually the same issue.\textsuperscript{43} For example, the formation of a group is essentially another means of acquiring shares and may be viewed as a new owner under control share statutes. Accordingly, the open question remains the same: whether a control share acquisition occurs when an entity issues new voting shares to an existing controlling shareholder resulting in an increase in voting control over the statutory limit.\textsuperscript{44}

The \textit{Simon} case offers a prime example of how several state courts and model acts have addressed this question. Accordingly, Part I of this Article will address the \textit{Simon} court’s reasoning, followed by a discussion of how several other states and model acts have addressed the same question. After highlighting some of the inconsistencies and unforeseen consequences the \textit{Simon} decision will have on current and future minority shareholders during tender offers, and how other courts and model acts have dealt with the same issue, Part II will address some of the legislative responses to cases such as \textit{Simon}. Part III will describe why control share statutes on their face should apply to newly issued shares, even if courts are not applying the statutes in this fashion. Moreover, Part III will analyze why excluding newly issued shares from control share statutes does not reduce coercion, entrenches incumbent management, and cuts against the intent of control share statutes, which were designed to level the playing field among bidders and holdout shareholders.

\begin{footnotesize}
\begin{enumerate}
\item Breaud, 657 So. 2d at 1343.
\item \textit{Atlantis Group}, Fed. Sec. L. Rep. (CCH) § 96,445 at 91,939.
\item \textit{Simon}, 240 F. Supp. 2d at 649.
\item The court in \textit{Simon} states that control share acquisitions mean one of two things: "either the 'acquisition, directly or indirectly, by any person of ownership of . . . issued and outstanding control shares . . .' or ' . . . the power to direct the exercise of voting power with respect to, issued and outstanding control shares." 216 F. Supp. 2d. 919, 941 (E.D. Mich. 2003). Nevertheless, the issue remains the same because any transaction in which a person or group acquires the substantive practical ability to vote or direct the voting power within the ranges specified in the Michigan Act will constitute a control share acquisition. See \textit{id.} at 942 (citing IND. CODE § 23-1-42-2, Official Comments).
\item \textit{See Mich. COMP. LAWS} § 450.1790(2) (2003) (stating the statutory limits of voting power that trigger the Michigan Act).
\end{enumerate}
\end{footnotesize}
I. THE VARIOUS INTERPRETATIONS OF CONTROL SHARE STATUTES

A. Michigan

The issue facing the court in Simon was the Michigan Act's definition of a control share acquisition in the context of the phrase "issued and outstanding." Under the Michigan Act, a "control share acquisition" means the acquisition, directly or indirectly, by any person of ownership of, or the power to direct the exercise of voting power with respect to, issued and outstanding control shares. After recognizing that there is limited case law interpreting the Michigan Act, and none dealing with the specific question raised, the court in Simon turned to the Indiana Act for assistance in interpreting the Michigan Act. In support of TCI's position that the phrase "issued and outstanding" applies only to issued and outstanding shares, the court cites a single brief statement from the Official Comments from the Indiana Act:

Because "control share acquisition" is defined as the acquisition of already "issued and outstanding" control shares, a person's acquisition from the corporation itself of shares that were previously not issued or outstanding (such as newly authorized shares, or treasury shares being reissued) will not constitute a "control share acquisition," even if the acquisition puts that person over one of the [Ind. Code § 23-1-42-1's] three thresholds of voting power. However, that person's acquisition of the same number of shares in a public offering (rather than directly from the corporation) would constitute a "control share acquisition," since the shares will already have been "issued" (to an underwriter) before being acquired by that person.

The court dismissed SPG’s argument that the Michigan Legislature intended for the Michigan Act to apply to newly issued shares and found that by adopting language similar to that of the Indiana Act, it was proper to infer that the Michigan Legislature adopted the intent of the Indiana Legislature as well. Therefore, the...
court found that issuing the Series B stock was not a control share acquisition within the meaning of the Michigan Act.51

Michigan courts have also previously relied on the Indiana Act when interpreting the Michigan Act, specifically when interpreting the definition of the term group.52 The Official Comments to the Indiana Act offer guidance in defining the term group, because neither the Indiana Act nor the Michigan Act defines the term.53 The Official Comments state that the Indiana Legislature’s approach was similar to that adopted in section 13(d) of the Securities and Exchange Act.54 Accordingly, the court in Simon cites several well-established factors in determining the existence of a group: (i) whether there is either a formal or informal understanding between individuals for the purpose of acquiring or holding securities; (ii) whether there were representations to third parties by members of a group that they together control a block of shares, even though those shares are registered with the company as being owned by individuals; and (iii) the action the group takes that affects the corporate direction of the company.55

In applying these facts, the court quickly finds sufficient evidence to infer the formation of a group. First, the court notes that the Taubman family and other shareholders gave Robert Taubman sole and absolute authority to vote their shares through voting agreements.56 Second, friends of the Taubman family exercised options and subsequently granted Robert Taubman sole authority to vote their shares.57 Third, and most damaging, the Schedule 13D filed by the Taubman family clearly indicates that as a result of the various transactions and agreements the Taubman family controlled a 33.6% interest in TCI and the members of the group entered these agreements for the purpose of preventing an unsolicited takeover of the company.58

Despite the court’s reliance on the Indiana Act, the language in the Michigan Act does not clearly include or exclude shares issued directly to incumbent management. Nevertheless, the Michigan courts have decided to follow the reasoning of the Indiana Legislature and courts.

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51. Id. at 648–49.
52. Id. at 648 (citing Atlantis Group, Inc. v. Alizac Partners, Fed. Sec. L. Rep. (CCH) ¶ 96,445 at 91,940 (W.D. Mich. 1991)).
53. Id. at 649.
54. Id. (citing 15 U.S.C. § 78 et seq. (2000)).
57. Id.
58. Id.
B. Indiana

Similar to the Michigan court, the Indiana Supreme Court in *Young v. General Acceptance Corp.* upheld a lower court’s finding that newly issued shares, which were not part of the common stock that was issued and outstanding, were not subject to the control share statute. In *Young*, Conseco Inc. pursued a tender offer to acquire General Acceptance Corp. (GAC) by entering stockholders’ agreements and securities purchase agreements. A subsidiary of Conseco would invest a large sum of money in return for subordinated convertible notes. These notes, in turn, would be convertible into common shares of GAC upon proper written notice. Before these agreements were entered into, there were roughly six million shares of GAC common stock outstanding, and of those shares, roughly thirty percent were owned by public shareholders, with the remaining seventy percent being owned by the Algood family or family trusts. Just before Conseco made a merger proposal to GAC, Conseco had acquired almost four million shares of GAC.

The court in *Young* quickly found that by definition the shares acquired by Conseco from GAC were not subject to the Indiana Act. Similar to the court in *Simon*, the court in *Young* also found that stockholder agreements were “interested shares” under the Indiana Act because Conseco held the ultimate power to exercise or direct the voting power of the shares subject to the stockholder agreements. The court reasoned that the stockholder agreements were different from a revocable proxy because the commitments to vote were given for consideration and became enforceable obligations. Nevertheless, the court in *Young* found an exception to the Indiana Act because there was no fundamental change in the nature of the corporation when Conseco acquired its control shares from GAC. Therefore, the common shareholders were not disadvantaged.

The court in *Young* found that the statute was intended to disenfranchise control shares in a hostile takeover or similar transaction where the transaction causes the entity to become dominated by a single shareholder or group of shareholders. Before Conseco’s acquisition, GAC was controlled by the Algood family. Therefore, the court reasoned that Conseco’s acquisition of control shares did not shift GAC into a corporation dominated by a single shareholder; rather, GAC had always been dominated by a single shareholder. In sum, although the court in *Young* found

59. 770 N.E.2d 298 (Ind. 2002).
60. *Simon*, 240 F. Supp. 2d at 647 (citing *Young*, 770 N.E.2d at 301).
61. 770 N.E.2d at 302.
62. *Id.*
63. *Id.*
64. *Id.* at 303 (citing IND. CODE § 23-1-42-2(e) (2003)).
65. *Id.* See also Introductory Comment to IND. CODE § 23-1-42-1 -11 (stating that the purpose of the statute was to give shareholders a right to vote on “a potentially fundamental change in the nature of their corporation—namely, its shift to being an entity in which a single shareholder acquires a significant level of dominance”).
66. *Young*, 770 N.E.2d at 303.
that a transfer of voting power may occur through the sale of shares or by contract, the court held that the Indiana Act does not apply to instances where a corporation is controlled by a dominant shareholder who sells his dominant position to another.\(^7\)

The court's reasoning in *Young* is hard to reconcile with the plain language of the Indiana Act or virtually any other control share statute. The Indiana Act requires shareholder approval for all shares acquired above a certain percentage, for instance thirty-three percent.\(^8\) Moreover, the Official Comments, while not technically binding on courts, say the commission believed that the thirty-three percent threshold was necessary because such a block of shares was sufficient to constitute effective control of the company.\(^9\) Thus, it appears that the Indiana Act would govern a sale of control by a controlling shareholder such as the sale of control in *Perlman v. Feldmann*,\(^10\) which, in fact, involved an Indiana corporation.\(^11\)

In this sense, a sale of control is essentially equivalent to a partial bid by an outsider. For example, a purchaser may be motivated to pay a higher premium to the controlling shareholder in order to loot the company, or the purchaser may simply think he can make the company worth more and can gain control by having to deal only with the controlling shareholder.\(^12\) This result may be a mixed blessing for states with similar control share statutes.\(^13\) It seems only fair to apply the statute equally to all sales of control, but sales of control may become less frequent and more expensive as a result.\(^14\)

Nevertheless, control share statutes are ostensibly designed to reduce coercion by giving holdout shareholders a right to vote on any sale that will cause the corporation to become controlled by a single person or group. Therefore, it would make little difference if the company was previously controlled by a single person or group and subsequently sold to another controlling single person or group.\(^15\) In either case, there has been a fundamental shift in control and holdout shareholders are subject to the threat of coercion by such a sale. The basic question becomes whether control share statutes are designed to ensure a fair outcome between a bidder and holdout shareholders, or whether they are designed to protect local companies by expanding the voting power of incumbent management. Although it

\(^67\). *Id.*


\(^69\). *Id.* at § 23-1-42-1, Official Comment (2003).

\(^70\). 219 F.2d 173 (2d Cir. 1955).

\(^71\). Booth, supra note 1, at 1690.

\(^72\). *Id.*

\(^73\). *Id.*

\(^74\). *Id.*

\(^75\). The opening comment to § 23-1-42-1 of the Indiana Act states that "[t]he Control Share Acquisitions Chapter reflects the General Assembly's recognition that a single shareholder's acquisition of a controlling block of shares can be an equally fundamental, far-reaching event for the corporation" and "that it is appropriate for shareholders to vote collectively on this issue as well." IND. CODE § 23-1-42-1 cmt. (2003).
appears that Michigan and Indiana favor the latter interpretation, other states have taken a different position.

C. Utah

The Utah Supreme Court in *Business Aviation of South Dakota, Inc. v. Medivest, Inc.*, 76 offers a contradictory opinion to the Indiana Act's Official Comments. In *Business Aviation*, the Utah Supreme Court considered whether the Utah Control Act ("Utah Act") applied to the issuance of new shares.77 The plaintiffs in *Business Aviation* engaged an agent to assist in removing the current board of directors and filed a Schedule 13D. According to the Schedule 13D, the plaintiffs sought to remove the board of directors because shareholders questioned the board’s effectiveness in discharging its fiduciary duties by intending to obtain control of the company by soliciting proxies to elect new directors of the company. In response to the plaintiff’s filing a Schedule 13D, the Medivest, Inc., board issued more than 1,100,000 new shares to three current members of its board in order to maintain control of the company by increasing the current board’s percentage ownership of stock.

The defendants in *Business Aviation* made two arguments, similar to those made by TCI in *Simon*.78 First, the defendants argued that they were outside the purpose of the Utah Act, which they claimed sought to protect Utah corporations from hostile takeovers.79 Second, the defendants argued that the shares of stock the board was issued were newly issued shares, rather than “issued and outstanding shares,” to which the Act has no application.80

The Utah Supreme Court rejected the first argument by finding that nowhere in the Utah Act were the words *outside*, *hostile*, or *takeover* used.81 The Utah court emphasized that similarly, neither the Michigan Act nor the Indiana Act contains these terms.82 In reaching this conclusion, the court in *Business Aviation* reasoned that courts have no power to rewrite a statute to make it conform to an intention not clearly expressed in the text, but rather should look to the specific language used in the statute.83

76. 882 P.2d 662 (Utah 1994).
77. *Id.* at 664.
78. *Id.*
79. *Id.*
80. *Id.*
81. *Id.* at 664–65 (emphasis added).
83. *Business Aviation*, 882 P.2d at 665 (citing *In re Criminal Investigation*, 754 P.2d 633, 640 (Utah 1988)). The court also notes that the legislative history seems to indicate a more broad reading of the Utah Act, quoting a Representative who states that the Act would allow “existing independent shareholders to evaluate offers from both existing management and a proposed acquiring entity.” *Id.* at 664–65 n. 3 (emphasis omitted) (quoting Floor Debate, vote on S.B. 3, 47th Legis., 1st Special Sess. (May 20, 1987) (House of Representatives Recording No. 6)).
The court went on to address the defendant's second argument that the phrase "issued and outstanding" as used in the Utah Act does not apply to newly issued shares to incumbent management. The court found that a reading of the Utah Act excluding newly issued shares would be contrary to the intent of the Utah Act and that the exclusion

would improperly allow a board of directors to defeat any challenge to their control of a corporation by giving its members controlling voting power in the form of additional shares of stock whenever shareholders seek the election of a new board of directors. . . Here, defendants, by issuing new shares [to the three members of the board of directors] have changed the proportional voting power of Medivest in order to maintain control of the corporation. In taking such action, defendants have acquired the power to direct the exercise of the voting power of Medivest in violation of the Act.

One difference between Business Aviation and Simon is that the acquiring corporation, and not shareholders, filed suit in Simon. Nevertheless, the premise was the same. In both cases the control share statute was being used to prevent incumbent management from maintaining or gaining control of the corporation by issuing new shares to themselves. Control share statutes were designed to reduce coercion by ensuring a fair outcome between bidders and holdout shareholders through a requirement that shareholders vote on all sales of control.

As the court in Business Aviation recognized, coercion is not reduced by granting carte blanche authority to incumbent management to issue new shares to themselves whenever their positions become threatened or when they do not believe a tender offer is in the best interests of the corporation. While management surely has the right to express its displeasure or unsatisfactory opinion concerning a tender offer, a control share statute that excludes newly issued shares to directors allows for management to cement their positions and effectively grants management further control of the company in the form of an absolute veto right over many decisions. More simply put, such a result grants too much power to incumbent management and negates any attempts by shareholders to remove current management, remove corporate takeover defenses, or tender their shares in what the holdout shareholders' believe is a profitable tender offer. These are precisely the types of coercion that the control share statutes sought to prevent.

D. The Model Acts

The Model Control Share Act ("Model Act") echoes the similar position of the Business Aviation court regarding the exclusion of newly issued shares. The Model

84. Id. at 665.
85. Id.
Act states in a preliminary statement that "the Joint Committee [departs] from the Indiana Statute only for good reason." The commentary to section 3(e)(3)(K) of the Model Act adds that "an exclusion covering acquisitions of control shares directly from the corporation is viewed by the Joint Committee as unduly favoring management and evidencing a 'business protectionism' motivation, particularly [because] it can be used as a first step in a management buyout series of transactions." The Model Act is also at odds with the court in Young. The Model Act commentary says that perhaps the greatest difference "between the Model Act and the Indiana [Act] with respect to exclusions is that the Model Act does not contain an exclusion for the acquisition from another person of control shares as to which shareholders previously granted voting rights" in accordance with the Model Act. The commentary goes on to say, "it was the Joint Committee's determination not to include such an exclusion on the basis that the purposes of a control share statute have more to do with the identity, characteristics and plans of the specific acquiring person than with the block of stock." Further, the commentary states that shareholders collectively should determine whether the acquiring person should receive voting rights "based upon information contained in [a] disclosure statement." Finally, the Model Act says that "an undisclosed transferee of such person, who did not receive approval from the shareholders for the voting rights of the block of control shares, may be as objectionable to the shareholders as the prior control shareholder was unobjectionable." The Model Business Corporations Act (MBCA) also addresses the issue of newly issued shares. The MBCA requires shareholder approval for any issuance of shares where the voting power of the shares will compose more than twenty percent of the voting power of the shares of the entire corporation during a merger or acquisition. The MBCA, unlike the Indiana Act, does not eliminate the requirement of shareholder approval when the shares are newly issued. Accordingly, it seems to be consistent among the MBCA and the Model Act, which were enacted near the time of many control share statutes, that exempting newly issued shares leads to the entrenchment of management and does not reduce coercion in tender offers.

In sum, at least one court, the Model Act, and the MBCA have recognized some of the problems of having an exemption for newly issued shares. The potential problems of entrenching management, the lack of a reduction in coercion in tender offers, and business protectionism seem evident in the cases discussed in this Arti-

87. Id. at 712.
88. Id.
89. Id.
90. Id.
91. Id.
Newly Issued Shares & Control Share Statutes

cle. Still, they will likely occur in the future unless state control share statutes are amended. Nevertheless, state legislators appear to be taking the opposite position.

II. THE QUICK RESPONSE OF STATE LEGISLATURES

The true intent of control share statutes is arguable. In the wake of court decisions that reduced incumbent management’s power to maintain control of a corporation, however, the actions of state legislatures suggest that control share statutes were not passed with shareholder interests in mind, but as protectionist legislation. For example, less than one year after the decision in Business Aviation, the Utah Legislature amended its control share statute to specifically exempt shares issued directly from the corporation. The amendment essentially overruled the decision in Business Associations, thus limiting the ability of future shareholders to remove incumbent management. Similarly, less than a month after the court’s decision in Simon, the Michigan Senate submitted Senate Bill 218 to amend the Michigan Act.

Although Senate Bill 218 was never passed, submission of the bill offers further evidence of state legislatures’ business protectionist mentality and a lack of concern for shareholder rights. Senate Bill 218 does not specifically exempt shares issued directly from the corporation—it goes one step further and eliminates the need for shareholder approval on control share transactions altogether. Senate Bill 218 proposed to amend section 798(1) of the Michigan Act to enable the shareholders or board of directors to approve a resolution restoring the voting rights of shares acquired in a control transaction. Currently, voting rights may be restored by a majority of votes cast by shareholders entitled to vote. Under Senate Bill 218, however, the board of directors could have restored voting rights either by a vote “before or at the time of the control share acquisition, by a majority of the directors” or by a vote “after a control [transaction], by a majority of those directors in office at the time of the approval who also were directors at the time of the control share acquisition.”

Senate Bill 218 must be read in the context of the interested share provision in the Michigan Act, which prevents any acquiring person, any officers of the corporation, or any employees of the corporation who are also directors from voting their shares to reestablish voting rights to shares acquired in a control share transac-

95. Id. § 798(1).
98. Id. § 798(3)(b).
In sum, the current Michigan Act does not allow those persons with interested shares to vote to restore voting rights. Senate Bill 218, however, would have eliminated the need for a shareholder vote, thus eliminating the need to differentiate between interested shares and disinterested shares. A majority of the board of directors could simply issue shares to themselves to prevent a takeover and subsequently vote to restore voting rights in the control shares without ever seeking shareholder approval.  

Currently only disinterested outside directors can vote to restore voting rights, which at least somewhat reduces coercion and limits the possibility of entrenching management. Under Senate Bill 218, however, there would have been no distinction between outside and inside directors, and all that would have been required was a majority of the board’s approval to restore voting rights. For example, even if the court in *Simon* had held that shares issued directly from the corporation did constitute a control share acquisition, shareholders would not have had veto rights on whether the transaction went through. Rather, those directors who were previously considered interested parties, and could not vote to reestablish voting rights in the control shares, could simply vote to reestablish voting rights in their own transaction.

If the proposed amendment was passed, any control transaction would have the increased the likelihood of coercion because holdout shareholders would be more likely to tender their shares for fear that the board of directors would approve the transaction regardless of whether the shareholders approved of the transaction. More specifically, in a partial offer, coercion would be increased because holdout shareholders would face the prospect of holding shares in a captive company.  

Finally, Senate Bill 218 would likely have eliminated the ability of the Michigan Act to govern private sales of control because if a majority of the incumbent board, or even a single member of the board, possessed a controlling interest in the company, there would be no need for shareholder approval to authorize the sale of control. For example, if the controlling interest was held by a majority of the board, the majority would simply approve to restore voting rights to the acquirer. If the controlling interest was held by a single member of the board, it would be more difficult to get a majority vote. But it would be much easier than it would have been if the shareholders had the ability to veto the transaction. In either case, shareholders would have had no role, or a limited role, in restoring voting rights in private sales of control.

Although the Michigan Legislature never passed Senate Bill 218, it did enact Public Act 181 on September 18, 2003, in direct response to the litigation involv-
ing Simon Property Group, Inc., and Taubman Centers, Inc.\textsuperscript{104} Even though the litigation involving SPG and TCI involved two Michigan corporations,\textsuperscript{105} by passing Public Act 181 the Michigan Legislature nevertheless reassured shareholders in Michigan corporations that the Michigan Act is protectionist legislation and not designed to protect the rights of holdout shareholders or reduce coercion.\textsuperscript{106}

Public Act 181 amended section 791 of the Michigan Act to provide that “the formation of a group does not constitute a control share acquisition of shares of an issuing public corporation held by members of the group.”\textsuperscript{107} Public Act 181 also added section 798(a) to the Michigan Act to provide that “[s]hares without voting rights because the formation of a group after April 1, 1988 was deemed to be a control share acquisition shall have the same voting rights as were accorded the shares before the formation of the group.”\textsuperscript{108}

Apparently it was not enough that the Michigan Legislature passed Public Act 181 in direct response to the court’s decision in \textit{Simon} that the formation of a group does constitute a control share acquisition; the Michigan Legislature went one step further and added section 798a, which retroactively applied the new law to all decisions involving the formation of a group since the Michigan Act was first passed in 1988, including the court’s decision in \textit{Simon}.\textsuperscript{109} Accordingly, the Michigan Legislature effectively overturned the court’s decision in \textit{Simon} and ended any chance of SPG either winning its case or completing its acquisition of TCI.\textsuperscript{110}

Although the legislative analysis at the time of that the Michigan Act indicates that the Michigan Act was designed to ward off hostile takeover attempts, the quick and direct response of the Michigan Legislature to the court’s decision in \textit{Simon} sends a bad message to shareholders in Michigan corporations.\textsuperscript{111} Public Act 181 says it is unlawful for a single insider to evade a disinterested shareholder vote, but it is not unlawful for two or more people acting together to evade a disinterested shareholder vote.\textsuperscript{112} Such a change makes the Michigan Act easy to evade and goes against the Act’s intent.

In passing Public Act 181, the Michigan Legislature accepted the argument from proponents of the new law that takeovers reduce shareholder premiums and are bad for Michigan corporations and their shareholders. Such reasoning is incorrect. Shareholders in takeovers often receive higher premiums for their shares, and Pub-
lic Act 181 will reduce shareholder premiums by impairing shareholder rights and making it easier for the board of directors to reject higher offers for shares in order to maintain control of a corporation. For example, in the *Simon* case the newly amended Michigan Act would have made it easier for the board of directors of TCI to reject SPG's offer of twenty dollars per share for stock that was previously trading at fifteen dollars per share on the market. Finally, one critic of Public Act 181 who was involved in drafting the Michigan Act stated that the Michigan Act "was designed to provide shareholders of issuing public corporations an opportunity to have their voices heard when control of the corporation is at stake, so that the 'control premium' for shareholders of the corporation is not appropriated by a group of inside shareholders for their own benefit without any say-so from the other shareholders."

**III. Why Control Share Statutes Should Apply to Newly Issued Shares**

In any two-tier tender offer coercion is always a possibility because of the competing interests at work, yet courts and scholars appear to agree that coercive tender offers should not be prohibited. Courts have continually refused to rule that coercive tender offers are illegal; rather, they maintain that the purpose behind the Williams Act is to ensure a fair fight among the bidder and shareholders. Nevertheless, coercion remains a concern in any partial or two-tier tender offer. This section will briefly discuss the competing interests involved in two-tier tender offers, followed by a discussion on how control share statutes eliminate much of the coercion as long as the control share statutes include shares issued directly to incumbent management.

Shareholders like premiums. It is arguable that shareholders lose out in two-tier tender offers, but on average, shareholders as a whole appear to gain from all tender offers. The inherent coercive nature of any tender offer is that any premium is often viewed as better than no premium at all, thus holdout shareholders will tender their shares for fear that they will receive no premium at all. Yet in some situations shareholders will receive less than market value for their shares because they cannot negotiate as a group.

Shareholders are rarely, if ever, a cohesive and closely knit group. They are often dispersed across the country and lack the resources or methods of communication.
to coordinate their decisions as a whole.\textsuperscript{119} For example, in a front loaded two-tier tender, or even a partial tender offer targeted at individual shareholders, the holdout shareholders will likely perceive that their stock must be worth more because the bidder is willing to pay a higher price for their shares. Moreover, because they are unable to negotiate for a higher price as a group, the individual shareholders fear the prospect of being stuck with post-bid shares that are worth less. Thus, the only possible group to represent and negotiate on behalf of the shareholders is the board of directors.

Coercion will be reduced only if it is assumed that target management remains active and negotiates aggressively for a higher price, and of course is willing to lose control over the corporation if the takeover is successful. Inherent in this assumption is that shareholders depend on management to defend against what are perceived to be inadequate offers. Shareholders often oppose such defensive measures, however, and argue that such tactics are "designed to entrench management."\textsuperscript{120} Such opposition can be seen as evidence that shareholders on average believe tender offers to be beneficial, yet inherently distrust management. In short, a two-tier or partial tender offer will always involve the competing interests of shareholders who want a premium (of any amount) yet lack the capabilities to negotiate for the best price possible, and who also distrust management to negotiate in their best interests.

Control share statutes in general reduce coercion by requiring a vote on any transaction above a certain threshold, thus limiting the pressure to sell for fear of being relegated to a minority position.\textsuperscript{121} The ability of shareholders to veto a transaction will in most cases force the bidder to divulge the price and motivation for such an acquisition. Such a requirement allows shareholders to choose whether they wish to tender their shares on the belief that a sufficient premium has been offered, or to hold on to their shares on the belief that new management will make the corporation more profitable. In either case, control share statutes level the playing field and reduce coercion between bidders and shareholders by leaving the ultimate decision to holdout shareholders who are given the ability to negotiate as a group.

Control share statutes have two coercion-reducing functions: (i) sterilizing shares acquired beyond a certain threshold and (ii) precluding interested shareholders from voting to reinfranchise voting rights. These two functions are best discussed in tandem. The threshold levels at which control share statutes are triggered vary among the twenty-seven states that have controlled share statutes.\textsuperscript{122} Under most

\textsuperscript{119} Id. at 1647.
\textsuperscript{120} Id. at 1648.
\textsuperscript{121} Id. at 1679.
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statutes, control share acquisitions are triggered at three separate levels, twenty percent, thirty-three percent, and (a majority of all voting power) 50.1%.123 Moreover, most, if not all, control share statutes preclude interested shareholders from voting to restore voting rights to shares in a control share transaction. Interested shareholders most often include those persons acquiring shares in a control share acquisition, any officer of the issuing corporation, and any director of the issuing corporation who is also an employee.124 Thus, anytime a person or group acquires more than a certain percentage of shares, say thirty-three percent, only the disinterested shareholders are able to restore voting rights to those shares acquired in the control share acquisition.

The only persons besides public shareholders who are allowed to vote are those directors who are employees of the corporation.125 This requirement reduces coercion by limiting the competing interests between incumbent management who likely want to remain in control of the company, and shareholders who are seeking a premium, but who before control share statutes were unable to negotiate as a group.126 For example, in a management buyout the shareholders and management are adversaries and are not seeking the same results from the transaction. Thus, shareholder voting can act as a negotiating mechanism between management and shareholders, because a shareholders vote is equally valuable to the bidder and management and will likely lead to the shareholders’ receiving top dollar for their shares.127 Nevertheless, all the coercion-reducing factors between shareholders and management are eliminated if shares issued directly from the corporation are exempted under control share statutes.

A. The Unforeseen Consequences

Any tender offer will inevitably involve some coercion. Shareholders may tender their shares for fear of being paid less in the second step of the transaction, or they may tender their shares because they believe the offer is attractive.128 At the very least, in those states with control share statutes, “management and [the] bidder will present their best cases to the shareholders without the coercion and strategic behavior that [ordinarily] attends a tender offer.”129 But if control share statutes are intended to protect shareholders and reduce coercion, an exemption for newly issued shares to management would not ensure a fair outcome between inside management and holdout shareholders. Rather, such an exemption entrenches

125. MICH. COMP. LAWS § 450.1792 (2003).
126. IND. CODE § 23-1-42-3, Official Comment (2003) (stating that the General Assembly believed that inside directors also have other interests "threatened by [an] acquisition, such as preserving their positions [in] the corporation").
127. Booth, supra note 1, at 1684.
128. See id. at 1683.
129. Id.
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incumbent management and eliminates the ability of shareholders to tender their shares without the board of directors' approval.

The most obvious example of entrenchment that results from the exclusion of shares issued to incumbent management is the incumbent board's ability to issue itself new shares whenever they feel threatened by an outside corporation. Control share statutes were designed to sterilize a bidder, or any other twenty-percent shareholder, from assuming control of the company without shareholder approval, not management's approval. Yet, by exempting newly issued shares from control share statutes, inside management can issue new shares to itself and gain or maintain control of a corporation and effectively eliminate any protections the control share statutes offered shareholders. For example, suppose a current member of the board already controls a forty-percent interest in a company, with sixty percent being controlled by the remaining shareholders. If a person acquires a twenty-percent interest in a company, and the forty-percent controlling interest of the incumbent manager is allowed to vote, he will obviously vote to approve such a transaction because his forty-percent interest has just become a fifty-percent majority interest in the company. Before the bidder acquired the twenty-percent interest, the remaining shareholders retained control of the company, but by allowing the controlling interest holder to vote, there has been a fundamental shift in the nature of control. For this reason, control share statutes do not allow incumbent management to vote to restore voting rights, and should apply to shares issued to incumbent management.

CONCLUSION

Control share statutes were enacted to reduce coercion and ensure a fair outcome between bidders and holdout shareholders in tender offers. Unfortunately, the Simon court disregarded the intent behind control share statutes and found that the acquisition of newly issued shares from a corporation is not a control share acquisition within the meaning of the Michigan Act. By so ruling, the court in Simon grants too much power to incumbent management and negates any attempts by shareholders to tender their shares in what they believe to be a profitable tender offer.

In addition, the decision by the court in Simon coupled with the quick response from the Michigan Legislature in amending the Michigan Act and the decision by the Utah Legislature in amending the Utah Act, further supports the argument that control share statutes are being amended and interpreted with the idea of protecting local corporations, rather than protecting the interests of shareholders in tender offers. For example, Public Act 181 now makes it easier for incumbent management to evade the Michigan Act by simply forming a group. Shareholders, espe-

130. The Michigan Legislature clearly states that the Michigan Act is designed to protect Michigan corporations from hostile takeover attempts. H.B. 4764 Legislative Analysis (June 5, 2003).
cially those in Michigan corporations, are now less likely “to have their voices heard when control of the corporation is at stake,” such as when the control premium of the corporation is trying to be appropriated “by a group of inside shareholders for their own benefit without any [say] from the other shareholders.”

Control share statutes were designed to level the playing field and reduce coercion between outside bidders and shareholders by leaving the ultimate decision on whether a transaction goes through to the shareholders. Nevertheless, the court in *Simon*, other courts, and some state legislatures have eliminated many of the coercion-reducing factors within control share statutes by ruling or amending statutes to state that newly issued shares to incumbent management are exempt under control share statutes or that forming a group does not constitute a control share acquisition. In short, an exemption from control share statutes for newly issued shares to incumbent management eliminates many of the coercion-reducing factors inherent in control share statutes, entrenches current management by allowing them to issue shares to themselves whenever a takeover is threatened, and often makes it impossible for shareholders to tender their shares without the approval of the board of directors.

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