

January 1982

Tender Offer Manipulation: Tactics and Strategies after Marathon

Robert A. Profusek

Recommended Citation

Robert A. Profusek, *Tender Offer Manipulation: Tactics and Strategies after Marathon*, 36 Sw L.J. 975 (1982)

<https://scholar.smu.edu/smulr/vol36/iss4/2>

This Article is brought to you for free and open access by the Law Journals at SMU Scholar. It has been accepted for inclusion in SMU Law Review by an authorized administrator of SMU Scholar. For more information, please visit <http://digitalrepository.smu.edu>.

TENDER OFFER MANIPULATION: TACTICS AND STRATEGIES AFTER *MARATHON*

by

Robert A. Profusek*

"When I use the word," Humpty Dumpty said, in a rather scornful tone, "it means just what I choose it to mean—neither more nor less."

"The question is," said Alice, "whether you can make words mean so many different things."

"The question is," said Humpty Dumpty, "which is to be master—that's all."

L. Carroll, *Through the Looking-Glass*

THE tactics and strategies and, therefore, the legal considerations relating to unsolicited takeover bids have predominantly been designed and continually reshaped around the applicable state¹ and federal regulatory frameworks since the enactment of the Williams Act in 1968.² The approximately two-year period following the 1979 overhaul of the rules implementing the Williams Act³ by the Securities and Exchange Commission (SEC) has been no exception. That period witnessed a

* B.A., Cornell University; J.D., New York University. The author is a member of the Dallas office of Jones, Day, Reavis & Pogue.

1. For more than a decade, state takeover legislation was an important aspect of the structuring of almost any nationwide tender offer. *See generally* Shapiro, *State Takeover Laws*, 12 INST. ON SEC. REG. 401 (1980); 606 Sec. Reg. & L. Rep. (BNA) F-1 (June 3, 1981). The constitutional assault on these laws initially received a mixed response from the courts. *Compare* Great W. United Corp. v. Kidwell, 577 F.2d 1256 (5th Cir. 1978) (Idaho takeover statute invalid on supremacy and commerce clause grounds), *rev'd on venue grounds sub nom.* Leroy v. Great W. United Corp., 443 U.S. 173 (1979), *with* AMCA Int'l Corp. v. Krouse, 482 F. Supp. 929 (S.D. Ohio 1979) (Ohio takeover statute upheld against supremacy and commerce clause challenges). The assault recently culminated in *Edgar v. MITE Corp.*, 102 S. Ct. 2629, 73 L. Ed. 2d 269 (1982). In *MITE* a majority of the Supreme Court held that the Illinois takeover statute imposed an impermissible burden on interstate commerce. While certain features of the Illinois statute distinguish it from other state takeover laws (e.g., the Illinois statute provided for administrative review of the substantive fairness of tender offers subject to the statute), *MITE* may sound a death knell for virtually all state takeover legislation, at least as presently constituted. *See generally* Hanna Mining Co. v. Norcen Energy Resources Ltd., No. C82-959 (N.D. Ohio June 11, 1981) (pre-*MITE* decision adumbrating *MITE*'s analysis in holding that "penalty box" provision of Ohio Takeover Act, OHIO REV. CODE ANN. § 1707.041(B)(2) (Page Supp. 1981), was unconstitutional under commerce clause). In some part due to Justice Powell's concurrence in *MITE* (joining in the commerce clause ruling so as to permit the states room to legislate in the area), however, efforts have begun in a number of states to enact legislation that would withstand constitutional scrutiny.

2. 15 U.S.C. §§ 78m(d)-(g), 78n(d)-(f) (1976 & Supp. IV 1980).

3. SEC Securities Act Release No. 6158 (Nov. 29, 1979), [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,373.

proliferation of new tender offer tactics and strategies, which in significant part culminated in the battle between Mobil Corporation and United States Steel Corporation for control of Marathon Oil Company, and in the seemingly inevitable stockholders' litigation that resulted.⁴

This Article principally focuses upon the implications of litigation in which Mobil challenged asset and stock options granted by Marathon to U.S. Steel to induce the latter to make a competing offer, some 50% higher than Mobil's unsolicited bid, which Marathon's directors had rejected as "grossly inadequate."⁵ Mobil's challenge was essentially two-pronged:⁶ it alleged that (1) the granting of the options constituted a violation of the Marathon directors' state law fiduciary duties;⁷ and (2) the options were "manipulative" under section 14(e) of the Williams Act.⁸ After a four-day hearing on Mobil's application for a preliminary injunction, the trial court held that the challenged options were granted for a good faith business purpose (solicitation of a fair competing bid), and that the exercise price under each option was fair to Marathon's shareholders.⁹ Mobil, therefore, failed to make the required showing of likelihood of success on the merits.¹⁰ The trial court also held that the options could not be manipulative

4. In the interest of full disclosure, the author's firm, Jones, Day, Reavis & Pogue, acted as counsel for Marathon in connection with the Mobil/U.S. Steel/Marathon takeover battle and the stockholders' litigation resulting therefrom. The same firm also acted as counsel in the takeover bid by Norcen Energy Resources Limited for control of The Hanna Mining Company. See *infra* text accompanying notes 165-72. The views expressed herein are, of course, solely those of the author.

5. Marathon Oil Co. Statement on Schedule 14D-9, at 3 (Nov. 2, 1981).

6. See *infra* text accompanying notes 86-92. In addition to the breach of fiduciary duty and Williams Act theories, Mobil argued that the options granted to U.S. Steel were ultra vires and that the asset option constituted a sale of "substantially all" of Marathon's assets, thus allegedly requiring shareholder approval under OHIO REV. CODE ANN. § 1701.76 (Page 1978). See Complaint ¶¶ 34-47, Mobil Corp. v. Marathon Oil Co., No. 1402 (S.D. Ohio Nov. 19, 1982) [hereinafter cited as Complaint]. These allegations were not actively pursued in the hearing on Mobil's application for a preliminary injunction and were given short shrift by the trial court. Mobil Corp. v. Marathon Oil Co., [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,375 (S.D. Ohio), *rev'd on other grounds*, 669 F.2d 366 (6th Cir. 1981) [hereinafter cited as *Marathon*].

7. See Complaint, *supra* note 6, ¶¶ 30-34.

8. 15 U.S.C. § 78n(e) (1976); see Complaint, *supra* note 6, ¶¶ 24-29. Section 14(e) provides, in part, as follows:

It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request or solicitation.

9. *Marathon*, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,375, at 92,285.

10. *Id.* The trial court held (and the appellate court confirmed) that the standard for the issuance of a preliminary injunction in the Sixth Circuit was the traditional four-pronged test articulated in cases such as *Mason County Medical Ass'n v. Knebel*, 563 F.2d 256, 261 (6th Cir. 1977):

[In considering whether to grant a preliminary injunction, a trial court must consider the following factors:]

1) Whether the plaintiff has shown a strong or substantial likelihood or probability of success on the merits;

under section 14(e), because their existence and terms had been fully disclosed.¹¹ In a decision that, at the very least, came as a surprise to most members of the securities bar,¹² the Court of Appeals for the Sixth Circuit reversed the latter ruling and held that the options were "manipulative" under section 14(e) because they prevented other tender offer participants from "competing on a par . . . for control" of the subject company.¹³

This Article endeavors to analyze the principal legal and strategic implications of the *Marathon* concept of manipulation in the tender offer context. While the most obvious implications relate to the analysis of the legality of defensive measures implemented by the target or subject company, the *Marathon* holding may be most important in litigation instituted by the target against an unwanted bidder. Nonetheless, before *Marathon* and its implications can be properly analyzed, the legal and strategic stage upon which the case unfolded must be set forth so that its events can be considered in their proper context.

I. THE *MARATHON* SETTING

A. *On Offense*

1. *The SEC's 1979 Rules and the Demise of the State Takeover Laws.* In late 1979, after a series of false starts,¹⁴ the SEC implemented a major overhaul of the regulatory system under the Williams Act that was primarily designed to ensure prompt dissemination of and full disclosure relating to tender offers subject to the Act.¹⁵ Some of the new rules favor subject

-
- 2) Whether the plaintiff has shown irreparable injury;
 - 3) Whether the issuance of a preliminary injunction would cause substantial harm to others; [and]
 - 4) Whether the public interest would be served by issuing the preliminary injunction.

Marathon, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,375, at 92,275. A number of courts have relaxed the test for the issuance of preliminary injunctions in the tender offer context based upon a standard requiring the plaintiff to show either (1) probable success on the merits and possible irreparable injury or (2) sufficiently serious questions going to the merits to make them a fair ground for litigation and a balance of hardships tipping decidedly in the plaintiff's favor. See, e.g., *Missouri Portland Cement Co. v. Cargill, Inc.*, 498 F.2d 851, 871 (2d Cir.), cert. denied, 419 U.S. 883 (1974); *Alaska Interstate Co. v. McMillian*, 402 F. Supp. 532, 540 (D. Del. 1975); *Texasgulf, Inc. v. Canada Dev. Corp.*, 366 F. Supp. 374, 403 (S.D. Tex. 1973). The more relaxed standard has been held to be consistent with the Supreme Court's emphasis upon the applicability of "traditional equitable principles" in Williams Act litigation in *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 57-60 (1975). See, e.g., *Sea World, Inc. v. MCA, Inc.*, [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,803, at 90,912 (S.D. Cal. 1976).

11. *Marathon*, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,375, at 92,285.

12. Nathan, *Novel Legal Questions Explored*, Nat'l L.J., Mar. 29, 1982, at 25, col. 4; Bialkin, *Court Casts Cloud over Option Tactic in Takeovers*, Legal Times of Washington, Jan. 11, 1982, at 19, col. 1.

13. *Marathon*, 669 F.2d at 375.

14. See, e.g., SEC Securities Exchange Act Release No. 12,676 (Aug. 6, 1976), 41 Fed. Reg. 33,004; SEC Securities Act Release No. 5538 (Nov. 5, 1974), 39 Fed. Reg. 41,223; SEC Securities Act Release No. 5529 (Sept. 9, 1974), 39 Fed. Reg. 33,035.

15. SEC Securities Act Release No. 6158 (Nov. 29, 1979), [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,373.

companies. For example, rule 14d-7¹⁶ extends the minimum period during which the bidder must permit tendered shares to be withdrawn if desired by target shareholders to fifteen business days after the date of commencement of a takeover bid (plus ten additional business days following a competing bid); rule 14e-1(a) imposes a minimum offering period of twenty business days after commencement.¹⁷ Consistent, however, with most practitioners' perceptions of the SEC's biases in this area, the new rules on balance tend to favor bidders over subject companies. Thus, notwithstanding the substantial question of whether it had the power to do so,¹⁸ the SEC adopted rule 14d-5, which provides bidders an almost unfettered right to a subject company's shareholder list and security position listing.¹⁹ More importantly, on the stated ground that "pre-commencement public announcements cause security holders to make investment decisions with respect to a tender offer on the basis of incomplete information and trigger market activity normally attendant to a tender offer,"²⁰ the SEC adopted rule 14d-2(b),²¹ which requires the actual dissemination of a tender offer within five business days of the public announcement of its material terms.²² The immediate casualty was the preoffer waiting period require-

16. 17 C.F.R. § 240.14d-7 (1981).

17. *Id.* § 240.14e-1(a). The 20 business day offering requirement of rule 14e-1(a) is less significant from the subject company's perspective, because it only prescribes the period during which the bidder must accept properly tendered securities. Instead, the 15/10 business day withdrawal requirement of rule 14d-7 prescribes the critical period since it effectively fixes the date after which tendered securities may actually be purchased by the bidder.

18. *See generally* SEC Securities Act Release No. 6158 (Nov. 29, 1979), [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,373, at 82,587. While two courts had held prior to the promulgation of rule 14d-5 that bidders had a right to subject company shareholder lists, *Applied Digital Data Sys. Inc. v. Milgo Elec. Corp.*, 425 F. Supp. 1163, 1164 (S.D.N.Y. 1977); *Mesa Petroleum Co. v. Aztec Oil & Gas Co.*, 406 F. Supp. 910, 915 (N.D. Tex. 1976), the right had been limited to situations in which the subject company, facilitated by its exclusive possession of the list, had made false or misleading statements to shareholders. *See, e.g., A&K R.R. Materials, Inc. v. Green Bay & W.R.R.*, 437 F. Supp. 636 (E.D. Wis. 1977). It was generally held that, absent such circumstances, no right to the list was implicit in the Williams Act. *See, e.g., E. ARANOW & H. EINHORN, TENDER OFFERS FOR CORPORATE CONTROL* 15 (1973).

19. 17 C.F.R. § 240.14d-5 (1981). The subject company has the option to mail the bidder's tender offer materials if it does not wish to provide actual copies of its shareholder list and security position listing to the bidder. *Id.* § 14d-5(a). Most subject companies elect to conduct the mailing.

20. SEC Securities Act Release No. 6158 (Nov. 29, 1979), [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,373, at 82,582-83 (footnote omitted).

21. 17 C.F.R. § 240.14d-2(b) (1981).

22. A triggering public announcement under rule 14d-2(b) must disclose only (1) the identity of bidder and the subject company; (2) a statement of the class and amount of equity securities being sought; and (3) the price or range of prices being offered. *Id.* § 240.14d-2(c).

The SEC's stated concern for security holder protection in adopting rule 14d-2(b) has been challenged as a subterfuge for insuring the invalidation of state takeover laws. *See, e.g., Ohio v. SEC*, [1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,688 (S.D. Ohio 1980) (complaint dismissed on justiciability grounds). Indeed, if prevention of trading based upon a lack of full disclosure by the bidder had been the true aim of rule 14d-2(b), it would be difficult to justify the five business day hiatus between public announcement by the bidder and actual dissemination of tender offer materials permitted thereunder, the SEC staff's position that public announcement of the material terms of a tender offer by any person other than the bidder does not trigger rule 14d-2(b), SEC Securities Exchange Act Release

ments of the state takeover laws. As the SEC recognized in adopting rule 14d-2(b),²³ the so-called "commence or withdraw" requirements of the new rule made simultaneous compliance with the state-imposed waiting period requirements literally impossible.²⁴

Notwithstanding the fact that rule 14d-2(b) caused the only direct conflict between most state takeover statutes and the SEC's 1979 tender offer rules, the substantial thrust of the case law after the promulgation of those rules contravened the validity of the state laws.²⁵ Further, the bidder's institution of litigation without prior warning (precluding the subject company from choosing a favorable forum in which to litigate the state law issues) in order to obtain injunctive relief against the enforcement of state takeover laws replaced the "bear hug" offer and its variants as the preferred tactic of bidders in dealing with the state takeover laws.²⁶ *Marathon* was no exception.²⁷

No. 16,623 (Mar. 5, 1980), 3 FED. SEC. L. REP. (CCH) ¶ 24,284I, and the disparity in treatment between tender offers and other forms of business combination transactions in which prompt information dissemination is not required. See, e.g., Freund & Green, *Substance Over Form S-14: A Proposal To Reform SEC Regulation of Negotiated Acquisition*, 36 BUS. LAW. 1483 (1981).

23. SEC Securities Act Release No. 6158 (Nov. 29, 1979), [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,373, at 82,583-84.

24. Most states had required the bidder to make certain filings and notify the target company of its intentions for substantial periods prior to actual commencement of the tender offer. See, e.g., OHIO REV. CODE § 1707.041(B)(1) (Page 1976) (20 calendar day pre-offer filing and notification requirement). Thus, even as to state statutes having strong decisions upholding their constitutional validity, e.g., *AMCA Int'l Corp. v. Krouse*, 482 F. Supp. 929 (S.D. Ohio 1979), the promulgation of rule 14d-2(b) necessarily resulted in holdings that the state preoffer waiting period requirements were preempted. Compare *id.* with *Canadian Pac. Enters. (U.S.) Inc. v. Krouse*, 506 F. Supp. 1192 (S.D. Ohio 1981).

25. See, e.g., *Kennecott Corp. v. Smith*, 637 F.2d 181 (3d Cir. 1980); *MITE Corp. v. Dixon*, 633 F.2d 486 (7th Cir. 1980), *aff'd sub nom. Edgar v. MITE Corp.*, 102 S. Ct. 2629, 73 L. Ed. 2d 269 (1982). But see *Sharon Steel Corp. v. Whaland*, 50 U.S.L.W. 3998.18 (U.S. June 28, 1982), *vacating and remanding* 121 N.H. 607, 443 A.2d 1250 (1981) (judgment vacated in light of *MITE* decision); *Esmark, Inc. v. Strode*, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,238 (Ky. Ct. App. 1981). Ironically, the Supreme Court's decision in *MITE* was based upon commerce clause grounds only because the case arose prior to the effectiveness of rule 14d-2(b). See *supra* note 1.

26. "Bear hugs," commonly employed by bidders during the 1970s, were firm takeover offers, usually at substantial premiums over market, addressed to the subject company's directors, which were designed in part to avoid the state takeover laws by forcing public disclosure and thereby acceptance of the offer by the subject company. See, e.g., A. FLEISCHER, *TENDER OFFERS: DEFENSES, RESPONSES, AND PLANNING* 58 (1981); I M. LIPTON & E. STEINBERGER, *TAKEOVERS AND FREEZEOUTS* 111-15 (Supp. 1979).

27. *Mobil Corp. v. Marathon Oil Co.*, No. 1262 (S.D. Ohio Oct. 28, 1981). Although Mobil obtained injunctive relief in four other actions challenging the takeover laws of states having tangential contacts with Marathon or its business and assets, the United States District Court for the Southern District of Ohio refused to grant a temporary restraining order against the invocation of the Ohio Takeover Act, which clearly applied to Mobil's bid, since Marathon was organized under Ohio law. OHIO REV. CODE ANN. § 1707.041(B)(1) (Page Supp. 1981). The court reasoned:

The Ohio takeover statutes are entitled to presumptive validity. The Court believes that the decision concerning whether or not to grant injunctive relief respecting applicable state requirements can be properly made only after a hearing followed by thoughtful decision with findings of fact and conclusions of law concerning each of the relevant statutory components of the Act. Nothing in plaintiff's filings and nothing I have heard from counsel has convinced me that justice requires otherwise.

Rule 14d-2(b) and the demise of the state takeover laws operated in tandem to rekindle the "Saturday Night Special" tactic, which involved surprise tender offers structured around the minimum time frames legally permissible and offered at bargain prices because of the attendant decrease in the probability of competitive bidding.²⁸ At least some of these considerations probably affected Mobil's selection of tactics in its initial bid for control of Marathon. Other features of the SEC's 1979 tender offer rules also influenced Mobil's tactical choices.

2. Proration and Front-End Loading. The SEC's 1979 tender offer rules contain an apparent oversight. Although rule 14e-1 creates a twenty business day minimum offering period and rule 14d-7 creates a fifteen business day minimum withdrawal rights period, takeover bids comprised of part cash and part securities can still be structured, as in *Marathon*, in order to take advantage of the ten calendar day minimum proration period of section 14(d)(6).²⁹ The purpose of these takeover bids is to pressure target shareholders into tendering within the ten calendar day proration period to ensure that they will receive cash for at least a portion of their shares.³⁰ The pressure to tender during this period is particularly great when (1) the second-step, clean-up transaction contemplates securities of an undeterminable or clearly lower value; (2) substantial arbitrage activity is expected because of the practical advantages possessed by arbitrageurs and professional investors;³¹ or (3) competitive bidding is likely to occur.³²

Thus, front-end loading, bids in which the tender offer price is higher

Mobil Corp. v. Marathon Oil Co., No. 1262 (S.D. Ohio Nov. 10, 1981) (interim order).

28. See M. LIPTON & E. STEINBERGER, *supra* note 26, at 111. The Ohio Takeover Act's 60-day administrative review period preserved in AMCA Int'l Corp. v. Krouse, 482 F. Supp. 929 (S.D. Ohio 1979), not only afforded the target company the opportunity to challenge the disclosures in the initial bidder's proposed tender offer materials, but also gave the target company the time to locate a more favorable bidder, or "White Knight," offering almost \$100 million more than the initial bid. See Bendix Corp. Supplement To Offer To Purchase 2 (Dec. 17, 1979).

29. 15 U.S.C. § 78n(d)(6) (1976). Section 14(d)(6) requires that shares tendered within the first ten calendar days of a partial tender offer be purchased pro rata if more shares are tendered than the bidder is willing to purchase.

30. See, e.g., Lederman & Vlahakis, *Pricing and Proration in Tender Offers*, 14 REV. SEC. REG. 813, 818 n.28 (1982). The SEC's oversight probably resulted from the fact that the 1979 tender offer rules contemplated the "any or all" cash tender offer, which predominated during the immediately preceding period. Part cash, part stock offers can be attractive in the current economic environment given the present high interest rates and relative unattractiveness of the public securities markets to potential issuers. Gun-jumping problems under § 5 of the Securities Act of 1933, 15 U.S.C. § 77e (1976), have been effectively eliminated by an administrative interpretation of the SEC staff that purports to harmonize the requirements of that statute and the Williams Act. See SEC Securities Exchange Act Release No. 14,699 (Apr. 24, 1978), 3 FED. SEC. L. REP. (CCH) ¶ 24,284H.

31. See SEC Securities Exchange Act Release No. 18,761 (May 25, 1982), [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 83,222 (proposing rule 14d-8, which would require pro rata acceptance of all shares properly tendered); SEC Securities Exchange Act Release No. 18,050 (Aug. 21, 1981), [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 83,019 (proposed revision of rule 10b-4 to proscribe "hedged tendering").

32. In a competitive bidding situation the cash portion can be increased and the paper portion left at the initial level or only slightly increased as in Mobil's counter-bids for Conoco, Inc. in 1981.

than the price contemplated by the squeeze-out merger, can be said to undermine the fifteen and twenty business day periods of rules 14d-7 and 14e-1(a), and the tactic is designed to pressure target shareholders into tendering early. Nothing in the SEC's rules, however, at least as presently constituted,³³ prohibits the practice. Further, in *Radol v. Thomas*,³⁴ the consolidated shareholders' litigation seeking to enjoin the U.S. Steel—Marathon merger, Judge Rubin held that front-end loading was not manipulative under section 14(e) or rule 10b-5³⁵ in light of the implicit recognition of such transactions in the SEC's rules³⁶ and of the evidence adduced in the hearing on plaintiff's motion to enjoin the merger "that the overwhelming response to U.S. Steel's tender offer was due, not to the coerciveness alleged to be inherent in a two-tier pricing structure, but because of the relatively attractive price offered at both ends of the transaction."³⁷ However, absent Mobil's initial bid for Marathon (some fifty percent less than U.S. Steel's counterbid), predicting whether the outcome in *Radol* would have been different is impossible.

Not only had target companies such as Marathon effectively lost the protections of the state takeover statutes and the relative luxury of time they had afforded, but also many target company shareholders, particularly nonprofessional investors, had to confront the decision of whether or not to tender within the short time period of section 14(d)(6). One unrelated factor, which is not susceptible to substantiation by case or rule citations, but is nonetheless significant to an analysis of the offensive setting prior to *Marathon* is the clearly perceptible shift in antitrust enforcement attitudes that accompanied the current Administration into office.

3. *Shift in Antitrust Enforcement Attitude in Washington.* The notification and regular review procedures of the Hart-Scott-Rodino Antitrust Improvements Act of 1976³⁸ have greatly aided the subject company in efforts to persuade the Department of Justice (DOJ) or the Federal Trade Commission to consider challenging takeover bids on antitrust grounds, particularly those attempts delayed due to the operation of state takeover laws. However, given the relatively lax antitrust enforcement attitudes of the

33. The SEC's proposed rule 14d-8, SEC Securities Exchange Act Release No. 18,761 (May 25, 1982), [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 83,222, if adopted, will alleviate some of the pressure by requiring proration with respect to all shares tendered during the period of a tender offer. Some front-end loading would probably remain since the practice can still reduce the overall cost of an acquisition and because, as a practical matter, not all target stockholders (e.g., some nonprofessional investors) will accept any tender offer.

34. [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,693 (S.D. Ohio 1982).

35. 17 C.F.R. § 240.10b-5 (1981).

36. Rule 13e-3 provides an exception from the SEC's going-private disclosure rules for second-step transactions consummated within a year of a tender offer provided that target shareholders receive equal consideration in the second step. *Id.* § 240.13e-3. "Rule 13e-3 thus, by negative implication, acknowledges that such transactions occur and purports to regulate the second step of such two-tier transactions." *Radol v. Thomas*, [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,693, at 93,460 (S.D. Ohio 1982).

37. [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,693, at 93,460.

38. 15 U.S.C. §§ 1, 8, 15c, 18a, 1311 (1976 & Supp. IV 1980).

current Administration³⁹ and the reality of the DOJ's actions, or inactions in, for example, the 1981 attempted takeover of Grumman Corporation,⁴⁰ efforts actively to engage the regulatory agencies in Washington clearly became a secondary antitrust strategy to the preferred approach of private litigation in the hustings.

The shift in governmental antitrust enforcement attitudes in Washington also played a significant role in *Marathon*; it is unlikely that Mobil's offer would have been attempted without the shift.⁴¹ Before that litigation can be analyzed directly, however, the principal pre-*Marathon* development on defense should be briefly considered. That development marked the evolution of the target company's duties to resist an inadequate or illegal takeover bid.

B. On Defense

1. *Defensive Strategies Generally.* A successful tender offer defense based upon alleged securities law violations depends in part upon the current events in the securities law field,⁴² amendments to the SEC's Williams Act rules,⁴³ and various factual issues such as disclosure of regulatory impediments to the offer,⁴⁴ pending litigation,⁴⁵ possible conflicts of interest,⁴⁶ bidder access to inside information,⁴⁷ and plans and purpose disclosure.⁴⁸ Prevalent substantive defense strategies include the invocation of state takeover statutes that, at least prior to *Edgar v. MITE Corp.*,⁴⁹ withstood constitutional attack,⁵⁰ "scorched earth,"⁵¹ procurement of a "White

39. See U.S. Dep't of Justice and FTC Merger Guidelines—1982, [Extra Edition, June 16, 1982] TRADE REG. REP. (CCH) 9-54 (June 14, 1982). See generally Baker, *Justice Dept. Merger Guidelines Contribute a Dose of Rationality*, Nat'l L.J., June 28, 1982, at 16, col. 1.

40. Grumman Corp. v. LTV Corp., 527 F. Supp. 86 (E.D.N.Y.), *aff'd*, 665 F.2d 10 (2d Cir. 1981).

41. For example, Exxon Corporation's tender offer for Reliance Electric Company in 1979 was challenged by the Federal Trade Commission based upon the "potential entrant" theory. Reliance Electric Co. Proxy Statement 10-13 (Nov. 28, 1979). Prior to the current Administration, no major oil company had attempted a non-negotiated takeover of another fully integrated oil company.

42. See *Berman v. Gerber Prods. Co.*, 454 F. Supp. 1310 (W.D. Mich. 1978) (litigation relating to questionable payments).

43. See, e.g., *Life Investors, Inc. v. AGO Holding, N.V.*, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,356 (8th Cir. Oct. 21, 1981) (litigation relating to disclosure of bidder's financial statements); *Gray Drug Stores, Inc. v. Simmons*, 522 F. Supp. 961 (N.D. Ohio 1981) (litigation relating to meaning of "bidder").

44. See *Ronson Corp. v. Liquifin A.G.*, No. 785-73 (D.N.J. July 3, 1973), *aff'd per curiam*, 483 F.2d 846 (3d Cir. 1973), *cert. denied*, 419 U.S. 870 (1974).

45. See *SEC v. Texas Int'l Co.*, 498 F. Supp. 1231 (N.D. Ill. 1980).

46. See *Sonesta Int'l Hotels Corp. v. Wellington Assocs.*, 483 F.2d 247 (2d Cir. 1973).

47. See *Crane Co. v. Westinghouse Air Brake Co.*, 419 F.2d 787, 796 (2d Cir. 1969) (rule 10b-5), *cert. denied*, 400 U.S. 822 (1970); *Flynn v. Bass Bros. Enters., Inc.*, 456 F. Supp. 484, 491-92 (E.D. Pa. 1978); see also *General Portland Inc. v. LaFarge Coppee S.A.*, No. CA-3-81-1060-D (N.D. Tex. Aug. 28, 1981).

48. See *Hanna Mining Co. v. Norcen Energy Resources Ltd.*, No. C82-959 (N.D. Ohio June 11, 1982).

49. See *supra* note 1.

50. See *AMCA Int'l Corp. v. Krouse*, 482 F. Supp. 929 (S.D. Ohio 1979).

51. See *In re Occidental Petroleum Corp.*, No. 041-15 (Ohio Div. of Secs. Oct. 9, 1978). "Scorched earth" defenses involve threatened sales of target company assets, extraordinary

Knight,"⁵² and, most importantly, antitrust litigation.⁵³

No fundamentally new defensive strategies predated *Marathon*. A general refinement of the White Knight approach (the "lock-up" techniques at issue in the case) and considerable administrative and decisional law on the federal and state duties of subject companies and their directors in the context of unsolicited takeover bids had emerged prior to *Marathon*. These developments, coupled with the SEC's inadvertent reincarnation of the Saturday Night Special approach to structuring takeover bids, required subject companies and their directors to make major strategic decisions in short time periods and to be prepared to make full disclosure to the public in order to justify their actions. These new disclosure requirements are considered first.

2. *New Subject Company Disclosure Requirements.* Prior to the promulgation of the SEC's 1979 tender offer rules, the Williams Act had been construed not to impose any obligation on the subject company to respond to a tender offer.⁵⁴ Subject companies did, of course, frequently publish press releases and advertisements with respect to takeover bids, and to that extent were subject to the filing requirements of rule 14d-9⁵⁵ and the general antifraud provisions of section 14(e).⁵⁶ In fact, subject company management had been held to a stricter standard of disclosure than the bidder because of state law fiduciary obligations and, at least with respect to some issues, the subject company's relatively greater access to information about itself and its plans.⁵⁷

The SEC's 1979 amendments include a wholesale revision of schedule 14D-9 (formerly denominated schedule 14D), the subject company's basic SEC disclosure form.⁵⁸ The amendments include the adoption of rule 14e-2(a),⁵⁹ which requires that the subject company publish a statement dis-

dividends by the target, and similar practices designed to make the target less attractive to an unwanted bidder.

52. "White Knights" are companies by which an initial target company agrees to be acquired to defeat an unwelcomed bidder, usually on terms providing substantially greater returns to target company shareholders. *See, e.g.*, Wall St. J., Sept. 24, 1982, at 3, col. 2 (reporting agreement in principle between Allied Corporation and The Bendix Corporation ending Martin-Marietta Corporation's takeover bid for Bendix).

53. *See generally* A. FLEISCHER, *supra* note 26, at 119-55.

54. *See, e.g.*, A&K R.R. Materials, Inc. v. Green Bay & W.R.R., 437 F. Supp. 636, 644 (E.D. Wis. 1977); E. ARANOW, H. EINHORN & G. BERLSTEIN, DEVELOPMENTS IN TENDER OFFERS FOR CORPORATE CONTROL 79-80 (1977).

55. 17 C.F.R. § 240.14d-9 (1981). Subject companies were not required to file under rule 14d-9 with respect to "stop-look-and-listen" communications. *Id.*

56. *See, e.g.*, Missouri Portland Cement Co. v. Cargill, Inc., 498 F.2d 851, 874-75 (2d Cir.), *cert. denied*, 419 U.S. 883 (1974); Humana, Inc. v. American Medicorp, Inc., [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,286 (S.D.N.Y. 1978); Alaska Interstate Co. v. McMillian, 402 F. Supp. 532 (D. Del. 1975).

57. *See, e.g.*, Flynn v. Bass Bros. Enters., Inc., 456 F. Supp. 484, 491-92 (E.D. Pa. 1978); Berman v. Gerber Prods. Co., 454 F. Supp. 1310, 1328-29 (W.D. Mich. 1978). *See generally* Chris-Craft Indus., Inc. v. Piper Aircraft Corp., 480 F.2d 341, 364-65 (2d Cir.) ("Corporate insiders therefore have a special responsibility to be meticulous and precise in their representations to shareholders."), *cert. denied*, 414 U.S. 910 (1973).

58. 17 C.F.R. § 240.14d-101 (1981).

59. *Id.* § 240.14e-2(a). Rule 14d-9(a), *id.* § 240.14d-9(a), requires the filing of a sched-

closing whether it recommends acceptance or rejection of the offer, whether it is remaining neutral with respect to the offer, or whether it is unable to take a position with respect to the offer. Item 4(b) of schedule 14D-9 now requires disclosure of the "reason(s) for the position (including the inability to take a position) stated." The instruction pursuant to item 4(b) expressly states: "Conclusory statements such as 'The tender offer is in the best interest of the shareholders,' will not be considered sufficient disclosure" ⁶⁰ Moreover, consistent with the SEC's general bias against defensive actions by target companies, ⁶¹ item 7 of schedule 14D-9 requires disclosure of "whether or not any negotiation is being undertaken or is underway by the subject company in response to the tender offer" relating to, inter alia, "[a]n extraordinary transaction such as a merger or reorganization, involving the subject company." ⁶² Subject company disclosures in response to these requirements have generally become very detailed and, although hard data is not available, the disclosure requirement has probably had a chilling effect on certain possible defensive responses to unsolicited takeover bids. At the same time state law imposed an affirmative duty upon target management to resist certain takeover bids, and practical realities required that the decision to determine a course of action be made within a very short time period.

3. *The Evolution of State Law Fiduciary Obligations in Opposing Unsolicited Takeover Bids.* It can be argued that tender offers constitute mere purchases and sales of securities of the target company in which the company and its management are not implicated. ⁶³ Although from humble beginnings, ⁶⁴ by the time *Marathon* was in the courts, the law had evolved that subject companies and their directors not only had the right, but had an affirmative duty to oppose takeover bids that would harm the corporate enterprise or that were inadequate from a financial point of view. ⁶⁵ Further, in an appropriate case that duty included an "affirmative [obligation]

ule 14D-9 with the SEC, with the exchange on which the subject company's equity securities are listed (or NASDAQ if such securities are traded over the counter), and with the bidder as soon as practicable on the date that any subject company solicitation or recommendation is first published, sent, or given to shareholders. Statements published pursuant to rule 14e-2(a) constitute solicitations or recommendations under rule 14d-9(a). Thus, schedule 14D-9 filings are now required for all tender offers subject to the Williams Act.

60. *Id.* § 240.14d-101. Prior to the adoption of schedule 14D-9 the SEC staff frequently commented upon the subject company's statement (or lack thereof) of reasons for a particular recommendation in schedule 14D filings. In practice that procedure rarely produced additional disclosures.

61. See, e.g., SEC Securities Exchange Act Release No. 15,230 (Oct. 13, 1978), [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,748 (setting forth SEC staff's views on required proxy statement disclosures in connection with shareholder approval of defensive measures).

62. 17 C.F.R. § 240.14d-101 (1981).

63. See generally *Edgar v. MITE Corp.*, 102 S. Ct. 2629, 73 L. Ed. 2d 269 (1982).

64. *Northwest Indus., Inc. v. B.F. Goodrich Co.*, 301 F. Supp. 706, 712 (N.D. Ill. 1969) ("[M]anagement has the responsibility to oppose offers which, in its best judgment, are detrimental to the company or its stockholders.").

65. See, e.g., *Heit v. Baird*, 567 F.2d 1157, 1161 (1st Cir. 1977); see also *Panter v. Marshall Field & Co.*, 646 F.2d 271, 297 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981); *Treadway Cos. v. Care Corp.*, 638 F.2d 357, 382-83 (2d Cir. 1980); *Crouse-Hinds Co. v. InterNorth*,

not to refrain from bringing actions" to stop an illegal tender offer.⁶⁶

A corollary to the affirmative duty to oppose an inadequate or illegal tender offer states that actions taken in fulfillment of that duty will be presumed to be valid and protected by the business judgment rule.⁶⁷ The business judgment rule should apply in this context even if it can be shown that one of the purposes for a defensive action is the retention of management in office because, "if *any* rational business purpose can be attributed to [management's] decision," it will not be second-guessed by the courts.⁶⁸ Only if the sole or primary purpose of a particular action is personally motivated will management bear the burden of proving that the transaction is intrinsically fair. As recently stated by the Court of Appeals for the Third Circuit: "[I]f actions are arguably taken for the benefit of the corporation, then the directors are presumed to have been exercising their sound business judgment rather than responding to any personal motivations."⁶⁹

Five significant decisions that applied the business judgment rule to the sale or granting of options to sell stock or assets predated *Marathon*. The most recent of these decisions, *Conoco, Inc. v. Mobil Oil Corp.*,⁷⁰ was strikingly similar to *Marathon*. Mobil, vying with E.I. duPont de Nemours & Co. to gain control of Conoco, sought a temporary restraining order against duPont's competing tender offer based upon a claim that a stock option entered into by Conoco and duPont constituted a breach of fiduciary duty and a waste of corporate assets by Conoco's directors. Judge Pierce, however, denied Mobil's application after reviewing the grant of the stock option under the business judgment rule. Since the option was presumed to be valid under the rule's application, Mobil was unable to rebut that presumption and to demonstrate the requisite likelihood of success on the merits.⁷¹

In two recent cases involving contests for control, the Second Circuit Court of Appeals reached similar results in considering the sale of blocks of stock accompanying the signing of merger agreements. In *Crouse-Hinds Co. v. InterNorth, Inc.*⁷² the Second Circuit reversed a trial court order granting the defendant bidder an injunction to halt the exchange of a block of target company stock for stock of a third company with which the

Inc., 634 F.2d 690, 702 (2d Cir. 1980); *Conoco, Inc. v. Mobil Oil Corp.*, No. 4787 (S.D.N.Y. Aug. 4, 1981); *GM Sub Corp. v. Liggett Group, Inc.*, No. 6155 (Del. Ch. Apr. 25, 1981).

66. *Berman v. Gerber Prods. Co.*, 454 F. Supp. 1310, 1323 (W.D. Mich. 1978).

67. See, e.g., *Crouse-Hinds Co. v. InterNorth, Inc.*, 634 F.2d 690, 701 (2d Cir. 1980) ("The starting point for analysis of an attack by a shareholder on a transaction of the corporation is the business judgment rule.").

68. *Kaplan v. Goldsamt*, 380 A.2d 556, 568 (Del. Ch. 1977) (emphasis added); see also *Whittaker Corp. v. Edgar*, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,483, at 92,833-34 (N.D. Ill.), *aff'd mem.*, Nos. 1305 & 1307 (7th Cir. March 5, 1982). But see *Mobil Corp. v. Marathon Oil Co.*, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,375 (S.D. Ohio) (putting burden of proof on defendant directors), *rev'd on other grounds*, 669 F.2d 366 (6th Cir. 1981).

69. *Johnson v. Trueblood*, 629 F.2d 287, 292 (3d Cir. 1980), *cert. denied*, 450 U.S. 999 (1981).

70. No. 4787 (S.D.N.Y. Aug. 4, 1981).

71. *Id.* at 11.

72. 634 F.2d 690 (2d Cir. 1980).

target had agreed to merge. The court acknowledged "the prudent recognition that courts are ill equipped and infrequently called on to evaluate what are and must be essentially business judgments."⁷³ Based upon similar reasoning, in *Treadway Cos. v. Care Corp.*⁷⁴ the Second Circuit reversed an order enjoining the voting of a block of the target company's stock that had been sold to the target's chosen merger partner.⁷⁵

In *GM Sub Corp. v. Liggett Group, Inc.*⁷⁶ the Delaware Chancery Court denied a tender offeror's motion for a restraining order to enjoin the sale of a target's "prize asset." Plaintiff GM Sub charged that defendant Liggett's directors had breached their fiduciary duties, because they had approved the sale of Liggett's wholly owned subsidiary, Austin, Nichols & Co., Inc., to a French company for the purpose of thwarting GM Sub's tender offer and thereby maintaining Liggett's incumbent management. Noting that GM Sub had not withdrawn its offer despite the prospective sale of Liggett's "prize asset" and that the sale of the asset did not guarantee that control of Liggett would not change hands,⁷⁷ Chancellor Brown found that GM Sub had failed to demonstrate that it was likely to succeed in proving the sale was designed to perpetuate control rather than to allow Liggett's shareholders to realize fair value for their shares of Austin, Nichols & Co., Inc.⁷⁸ Finally, in *Panter v. Marshall Field & Co.*⁷⁹ the Court of Appeals for the Seventh Circuit held that a subject company's board of directors had acted properly and within the protection of the business judgment rule when it authorized corporate actions in opposition to a tender offer that it determined to be financially inadequate. Those actions included the institution of antitrust litigation against the unwelcome suitor and engagement in "defensive acquisitions."⁸⁰

While the SEC's 1979 tender offer rules and the attendant demise of the state takeover laws emphasized surprise, short-fuse takeover bids, state fiduciary obligations had been construed to impose upon target company management a duty to resist an inadequate or illegal bid, and federal law required meticulous disclosure of actions taken in fulfillment of that duty. At the same time the state law business judgment rule had been deemed applicable to protect management from potential liabilities arising out of actions initiated in the takeover context. The stage was thus set for Mobil's surprise bid for control of Marathon.

II. MARATHON

A. Factual Background

On October 30, 1981, Mobil announced its intention to make a cash

73. *Id.* at 702.

74. 638 F.2d 357 (2d Cir. 1980).

75. *Id.* at 382-83.

76. No. 6155 (Del. Ch. Apr. 25, 1981).

77. *Id.* at 4.

78. *Id.* at 5.

79. 646 F.2d 271 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981).

80. 646 F.2d at 297.

tender offer at \$85 per share for approximately 51% of Marathon's outstanding shares. A clean-up merger involving vaguely described Mobil debentures valued, in the opinion of Mobil's investment banker, at \$85 per share would follow the cash tender offer. Mobil made a weekend distribution of the tender offer materials and an antitrust position paper to arbitrageurs and to other professional investors. Mobil did not, however, actually disseminate its offer within the meaning of rule 14d-4⁸¹ prior to the commencement of litigation by Marathon that alleged violations of the antitrust laws. Just before midnight on Sunday, November 1, 1981, the Chief Judge of the District Court for the Northern District of Ohio entered a temporary restraining order based upon the antitrust allegations that barred Mobil from taking any steps to implement its tender offer.⁸² Following a five-day hearing, the district court issued a preliminary injunction against the consummation of the tender offer. The injunction was subsequently affirmed by the Court of Appeals for the Sixth Circuit.⁸³

Notwithstanding the successes in its antitrust case against Mobil, on November 18, 1981, Marathon entered into an acquisition agreement with U.S. Steel that provided for a cash tender offer at \$125 per share, almost 50% more than the price offered by Mobil, for approximately 51% of Marathon's shares to be followed by a clean-up merger involving U.S. Steel debentures with a face value of \$100 per share. At the request of and to induce U.S. Steel to make its competing bid,⁸⁴ Marathon granted two options to its White Knight. The first option was for slightly less than the 18½% New York Stock Exchange threshold for nonstockholder approved issuances of stock⁸⁵ immediately exercisable at \$90 per share. At that time this amount approximated the present value of the paper portion of U.S. Steel's offer and was \$5 per share more than Mobil's initial bid. The second option related to Marathon's "crown jewel," a 48% producing interest in the Yates Field in west Texas. The Yates Field option was exercisable at \$2.8 billion, but only in the event that a third party gained control of Marathon.

Mobil sued in the District Court for the Southern District of Ohio⁸⁶ to

81. 17 C.F.R. § 240.14d-4 (1981). Rule 14d-4 provides three alternative methods for disseminating a tender offer: (1) long-form publication of the entire offer in a newspaper of national circulation; (2) summary publication of an advertisement in such a newspaper announcing the tender offer (with an undertaking promptly to furnish copies of the offer to shareholders); and (3) mailing the offer to target shareholders under the provisions of rule 14d-5 relating to the target's shareholder list and security position listing.

82. *Marathon Oil Co. v. Mobil Corp.*, No. C81-2193 (N.D. Ohio Nov. 1, 1982) (interim order).

83. *Marathon Oil Co. v. Mobil Corp.*, 530 F. Supp. 315 (N.D. Ohio), *aff'd*, 669 F.2d 379 (6th Cir. 1981), *cert. denied*, 50 U.S.L.W. 3670 (U.S. Feb. 23, 1982).

84. *Mobil Corp. v. Marathon Oil Co.*, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,375, at 92,281 (S.D. Ohio), *rev'd on other grounds*, 669 F.2d 366 (6th Cir. 1981). Such options are normally referred to as "lock ups" because they are designed in part to discourage competing bidders from making offers for the target company, thus "locking up" the target company.

85. NYSE COMPANY MANUAL A-284 (1978).

86. The District Court for the Southern District of Ohio had no meaningful nexus to the transactions at issue. The judges of that court were, however, generally familiar with contested tender offers because of the relatively large number of cases involving the Ohio Take-

invalidate the options and then increased the cash portion of its original offer to Marathon to \$1 per share more than the cash portion of U.S. Steel's offer. Mobil advanced four theories: (1) that the options were manipulative under section 14(e) and that adequate disclosure had not been made with respect to them;⁸⁷ (2) that the granting of the options constituted a breach of fiduciary duties by Marathon's directors;⁸⁸ (3) that the Yates Field option involved a sale of "substantially all" of Marathon's assets, thus requiring stockholder approval under state law,⁸⁹ since the Yates Field was clearly Marathon's most important asset;⁹⁰ and (4) that the options were ultra vires.⁹¹ Mobil apparently overlooked the argument (which has yet to be tested elsewhere) that the asset and stock options were an integral part of the proposed merger and therefore could not be exercised unless approved by stockholders.⁹²

B. The District Court Decision

The thrust of Mobil's presentation to the trial court was its allegation that the Marathon directors had breached their fiduciary obligations in granting the options. With respect to this issue, Judge Kinneary wrongly (in view of the decisions cited by him⁹³) imposed the burden of proof on Marathon's directors, thus eschewing the business judgment rule on the facts sub judice:

Where the consummation of a proposed business combination carries with it the anticipation of perpetuating the control of the directors, a personal interest sufficient to shift the burden of proof is shown. . . . [S]elf-interest need not be the sole motivation of an act in order to cause a shift in the burden of proof.⁹⁴

Despite wrongfully allocating the burden of proof, Judge Kinneary found that the Marathon directors had affirmatively shown that the exercise price under each option was fair to Marathon's shareholders and that the grant

over Act, OHIO REV. CODE ANN. § 1707.041(B)(2) (Page Supp. 1981), and were known not to have the predispositions of some districts to avoid judicial intervention in such controversies.

87. Complaint, *supra* note 6, ¶¶ 24-29. The disclosure argument was never fully developed at trial, probably in light of the established principle that nothing in the federal securities laws requires disclosures of disparaging or speculative characterizations; rather, all that is required to be disclosed are the basic facts that permit the reader to draw informed conclusions. *E.g.*, *Panther v. Marshall Field & Co.*, 646 F.2d 271, 278 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981); *Missouri Portland Cement Co. v. Cargill, Inc.*, 498 F.2d 851, 873 (2d Cir.), *cert. denied*, 419 U.S. 883 (1974); *Conoco, Inc. v. Mobil Oil Corp.*, No. 81-4787 (S.D.N.Y. Aug. 4, 1981).

88. Complaint, *supra* note 6, ¶¶ 30-33.

89. *See* OHIO REV. CODE ANN. § 1701.76 (Page 1978).

90. Complaint, *supra* note 6, ¶¶ 34-39.

91. *Id.* ¶¶ 40-47.

92. *See* OHIO REV. CODE ANN. § 1701.79 (Page Supp. 1981).

93. *E.g.*, *Crouse-Hinds Co. v. InterNorth, Inc.*, 634 F.2d 690 (2d Cir. 1980).

94. *Mobil Corp. v. Marathon Oil Co.*, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,375, at 92,284-85 (S.D. Ohio) (citations omitted), *rev'd on other grounds*, 669 F.2d 366 (6th Cir. 1981).

of the options was for a good-faith business purpose.⁹⁵ Accordingly, Judge Kinneary held that "Mobil has failed to demonstrate *any* likelihood or probability of success on the merits" on its fiduciary duty claim.⁹⁶

With respect to Mobil's manipulation theory, Judge Kinneary concluded:

The Court agrees with defendants that Mobil's claim as to the purpose and effect of the merger and option agreements amounts to no more than a claim that the Marathon directors acted unfairly and breached their fiduciary [duties] to Marathon and its shareholders. Such an allegation does not state a cause of action under Section 14(e).⁹⁷

In *Santa Fe Industries, Inc. v. Green*⁹⁸ the Supreme Court had held that deception or misrepresentation is a prerequisite for rule 10b-5 liability.⁹⁹ Accordingly, Judge Kinneary was "constrained to conclude" that the section 14(e) allegations presented "no, much less a strong or substantial, likelihood or probability of prevailing" on the merits.¹⁰⁰ Mobil then appealed Judge Kinneary's ruling to the Court of Appeals for the Sixth Circuit.

C. The Appellate Court Decision

In light of Judge Kinneary's strong factual findings with respect to the state law claims, Mobil switched its emphasis on appeal to its manipulation theory under section 14(e). In essence, Mobil argued that the "District Court erred in ruling that the 'lock-up' agreements did not violate section 14(e) . . . [because those] agreements have prevented a public auction of Marathon stock, thus depriving Marathon shareholders of hundreds of

95. The Court has found that the Yates Field option price of \$2.8 billion was not unreasonable. Further, the stock option price of \$90 per share was higher than both the then-current trading price of Marathon shares and the tender offer price of Mobil at \$85 when this option was given to [U.S. Steel's acquisition subsidiary]. The Court must conclude that both options were fair with respect to their valuation.

The Court also finds that defendants had a reasonable corporate purpose in granting the options. That purpose was to obtain the best possible deal for Marathon shareholders in the face of an inevitable takeover. . . . The record is replete with evidence that the directors thoroughly reviewed the alternatives open to them, diligently investigated the relevant facts, and relied upon the advice of competent professional advisors before accepting the agreements. In sum, the Court concludes from the evidence before it that the defendant directors have borne their burden of showing fairness, corporate purpose, and good faith.

[1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) at 92,285.

96. *Id.* (emphasis added).

97. *Id.* at 92,281.

98. 430 U.S. 462 (1977).

99. Except for their respective "in connection with" clauses, rule 10b-5 and section 14(e) are substantively identical. *See, e.g.,* *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579, 605 (5th Cir.), *cert. denied*, 419 U.S. 873 (1974); *Bucher v. Shumway*, [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,142, at 96,299 (S.D.N.Y. 1979), *aff'd*, 622 F.2d 572 (2d Cir.), *cert. denied*, 449 U.S. 841 (1980); *In re Sunshine Mining Co. v. Securities Litig.*, [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,217, at 96,635-36 (S.D.N.Y. 1979).

100. [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,375, at 92,282.

millions of premium dollars for their shares."¹⁰¹ Based upon the Supreme Court's holding in *Green*¹⁰² and upon Judge Kinneary's decision, the Marathon directors argued that "*misrepresentation or nondisclosure* is an essential element of a cause of action under Section 14(e),"¹⁰³ and that the trial court's factual finding that the challenged options were fair and for a good faith business purpose under state law precluded a finding that the Williams Act had been violated.¹⁰⁴ The issue was thus joined on appeal.

The appellate court did not disturb Judge Kinneary's rulings with respect to the fiduciary duty claims.¹⁰⁵ Nonetheless, it concluded that "the Yates Field option and the stock option individually and together are 'manipulative' as that term is used in section 14(e)."¹⁰⁶ The court reasoned:

In our view, it is difficult to conceive of a more effective and manipulative device than the "lock-up" options employed here, options which not only artificially affect, but for all practical purposes completely block, normal healthy market activity and, in fact, could be construed as expressly designed solely for that purpose.¹⁰⁷

The appellate court then analyzed each option individually. With respect to the stock option, the *Marathon* court concluded that its existence "prevents all others from competing on a par . . . for control of Marathon [and] serve[s] as an artificial and significant deterrent to competitive bidding."¹⁰⁸ The Yates Field option was also held to be manipulative because "[o]thers cannot compete on a par with [U.S. Steel]; its bid of \$125 per share thus amounts to an artificial ceiling on the value Marathon share-

101. Brief of Appellant Mobil Corp. at 16-17, *Mobil Corp. v. Marathon Oil Co.*, 669 F.2d 366 (6th Cir. 1981). Somewhat ironically, this argument, while ultimately relied upon by the appellate court, was founded on an inaccurate factual premise: Mobil was precluded from proceeding with its tender offer because of the injunction against it in Marathon's antitrust case, and no competing bidder other than U.S. Steel had emerged despite an exhaustive White Knight search by Marathon. The failure to find a more favorable bidder was probably due to the size of the transaction and the fact that most other major oil companies would face the same antitrust obstacles that Mobil had confronted. Accordingly, Judge Merritt dissented from the *Marathon* appellate ruling, stating: "[In] my view . . . Mobil's Williams Act case is moot in light of our disposition of the antitrust case." 669 F.2d at 378.

102. *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 479 (1977).

103. Brief of Appellees Marathon Oil Co. & Directors of Marathon Oil Co. at 25, *Mobil Corp. v. Marathon Oil Co.*, 669 F.2d 366 (6th Cir. 1981) [hereinafter cited as Appellees' Brief] (emphasis in original); see, e.g., *Panther v. Marshall Field & Co.*, 646 F.2d 271, 283 (7th Cir.), cert. denied, 102 S. Ct. 658 (1981); *Lewis v. McGraw*, 619 F.2d 192, 193 (2d Cir.), cert. denied, 449 U.S. 951 (1980); *Merritt v. Libby, McNeill & Libby*, 510 F. Supp. 366, 371 (S.D.N.Y. 1981).

104. Even if Mobil's interpretation of the Williams Act were correct, Mobil cannot prevail here because it has been found that the Marathon Directors have satisfied the highest obligation imposed by law—that of fiduciaries—to the very same persons—the Marathon shareholders—whom Mobil claims have been defrauded and manipulated under the Williams Act. If the Marathon Directors have satisfied the highest standard known to the law with respect to the transactions at issue, there is no basis in either law or fact for claiming that their conduct was fraudulent or manipulative under the Williams Act.

Appellees' Brief, *supra* note 103, at 3.

105. 669 F.2d at 374 ("We offer no opinion regarding the merits of the fiduciary duty claim . . .").

106. *Id.*

107. *Id.*

108. *Id.* at 375.

holders can receive for their shares.”¹⁰⁹

The *Marathon* court expressly rejected Judge Kinneary’s holding that the options could not be said to be manipulative under section 14(e) because they had not been accompanied by misrepresentation or deception:

It may be that the Marathon shareholders in this case have now been fully informed that their management granted . . . the Yates Field option and the stock option. They may now understand fully how these options deter any tender offers higher than \$125 per share. Yet, they have had no real alternative to accepting the . . . offer, because Mobil’s offer of \$126 is conditional upon the invalidity of the options, and there is and could be no other comparable tender offer as long as the “lock-up” options remain in effect. The artificial ceiling on the price of their shares at \$125 is manipulation to which they must submit whether it is disclosed to them or not, since in not tendering their shares . . . they risk being relegated to the “back end” of [U.S. Steel’s] takeover proposal and receiving only \$90 per share.

In short, to find compliance with section 14(e) solely by the full disclosure of a manipulative device as a *fait accompli* would be to read the “manipulative acts and practices” language completely out of the Williams Act.¹¹⁰

The appellate court, however, never confronted Marathon’s argument, which had clearly influenced the outcome in the trial court, that there could be no manipulation under federal law if the court affirmatively found that the challenged conduct satisfied the directors’ fiduciary obligations to subject company shareholders.¹¹¹ Rather, the appellate court merely noted that section 14(e) applied by its terms to “any person,” thereby implicitly suggesting that U.S. Steel’s demand and receipt of the options were manipulative even if the Marathon directors’ approval of their grant may not have also been demanded.¹¹² Accordingly, the appellate court ordered “that the tender offer of [U.S. Steel] of \$125 per share be kept open for a reasonable time but free of the inhibiting and unlawful impact of the two options which it extracted . . . as a condition of its agreement.”¹¹³

D. A Critique

Arguably, *Marathon* represents an impermissible extension of federal law and a concomitant unjustifiable intrusion into state law. In introducing the bill that was ultimately enacted as the Williams Act, the bill’s sponsor stated: “This legislation will close a significant gap in investor protection under the Federal securities laws by requiring the disclosure of pertinent information to stockholders when persons seek to obtain control of a corporation by a cash tender offer or through open market or privately

109. *Id.*

110. *Id.* at 376-77.

111. See *supra* text accompanying note 105.

112. 669 F.2d at 377. If the grant of the options was not manipulative under § 14(e), then comprehending how their receipt could be manipulative is difficult.

113. *Id.*

negotiated purchases of securities."¹¹⁴ Thus, the Williams Act is primarily a disclosure statute enacted for the benefit of security holders and is not intended to provide new substantive rights to either the bidder or the subject company: "The two major protagonists—the bidder and defending management—do not need any additional protection They have the resources and the arsenal of moves and countermoves which can adequately protect their interests."¹¹⁵

This factor principally led to the Supreme Court's conclusion in *Piper v. Chris-Craft Industries, Inc.*¹¹⁶ that a defeated bidder lacked standing to sue for damages under section 14(e). The Court noted that "tender offerors were not the intended beneficiaries" of the Williams Act.¹¹⁷ While the *Piper* Court was acutely aware that Congress did not intend to tip the balance in favor of the subject company or the bidder,¹¹⁸ it reasoned that this "express policy of neutrality scarcely suggests an intent to confer highly important, new rights upon the class of participants whose activities prompted the legislation in the first instance."¹¹⁹

The *Piper* Court utilized the four-pronged test articulated in *Cort v. Ash*¹²⁰ to analyze whether the inference of a private damage remedy under section 14(e) was appropriate. While not literally applicable to questions of whether, for example, a lock-up option or other defensive tactic violates section 14(e), the *Cort* analysis nonetheless seems relevant, because both issues relate to the ultimate scope and application of the Williams Act. The *Piper* Court readily concluded that the first two *Cort* factors, whether the plaintiff was a member of the "especial class" that the legislation was designed to protect and whether congressional intent to confer a right existed, militated against the inference of an action for damages since bidders were not the intended beneficiaries of the Williams Act.¹²¹ This conclusion would, of course, equally apply to a lock-up option, a defensive merger or, notwithstanding rule 14d-5, a request for the subject company's shareholder list. The third *Cort* factor inquires whether the inference of such a right would be consistent with the federal statutory scheme. The *Piper* Court concluded that "the Williams Act cannot consistently be interpreted as conferring a monetary remedy upon regulated parties, particularly where the award would not redound to the direct benefit of the protected class."¹²² Arguably, any defensive tactic other than disclosure that is undertaken to block an unsolicited offer (which was not the case in *Marathon* since the challenged options were necessary to solicit a higher

114. 113 CONG. REC. 854 (1967) (statement of Sen. Williams).

115. *Full Disclosure of Corporate Equity Ownership and in Corporate Takeover Bids: Hearings on S. 510 Before the Senate Subcomm. on Securities of the Senate Comm. on Banking & Currency*, 90th Cong., 1st Sess. 257 (1967) (statement of Prof. Hayes), *quoted in* *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1, 29 (1977).

116. 430 U.S. 1 (1977).

117. *Id.* at 28.

118. *Id.* at 29.

119. *Id.* at 30.

120. 422 U.S. 66 (1975).

121. 430 U.S. at 32 n.21.

122. *Id.* at 39.

bid) is inconsistent with the purposes of the Williams Act since, if effective, it might perforce prevent the consummation of a tender offer.

The fourth factor under *Cort* addresses whether the cause of action is one traditionally relegated to state law. Both in the *Piper* situation and in the *Marathon* context, state law has traditionally controlled. Furthermore, deference to state law was the principal policy consideration underlying the Supreme Court's refusal in *Santa Fe Industries, Inc. v. Green*¹²³ to extend rule 10b-5 to cover corporate conduct touching upon securities transactions that did not involve deception or manipulation. The *Green* Court stated that "[a]bsent a clear indication of congressional intent, we are reluctant to federalize the substantial portion of the law of corporations that deals with transactions in securities, particularly where established state policies of corporate regulation would be overridden."¹²⁴ Instead, the Court held that the word manipulation in rule 10b-5 is a term of art that "refers generally to practices, such as wash sales, matched orders, or rigged prices, that are intended to mislead investors by artificially affecting market activity."¹²⁵ Although the *Marathon* court paid lip service to *Green*, it ignored the latter's teaching that charges of corporate unfairness, absent deception, are not actionable under the federal securities laws.

Of course, a target company may have to disclose accurately the objective facts relating to a defensive act such as a merger.¹²⁶ Given that section 14(e) merely makes rule 10b-5 applicable to tender offers,¹²⁷ arguably the former should have no application in the absence of misrepresentation or failure to disclose material facts, or manipulation within the narrow meaning of *Green*. Judge Moore's dissent to the Second Circuit Court of Appeals' decision in *Green*¹²⁸ seems equally applicable in the tender offer context:

The [Second Circuit] majority's insistence on extending the federal securities anti-fraud provisions beyond the bounds of fraud and into the realms of fiduciary duty is disturbing enough. Accompanied, as it is, by their erroneous finding of a breach of such duty, and by the astonishing and impermissible establishment of a federal common law of corporations—as ill-founded as it is improper—disconcertion must give way to alarm.

...

... First and foremost, however, the point must be made that, in taking cognizance of plaintiffs' claim, the majority has not provided a remedy to correct a fraud; rather it has extended to these plaintiffs an

123. 430 U.S. 462 (1977).

124. *Id.* at 479.

125. *Id.* at 476. In *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199 (1976), the Supreme Court held: "Use of the word 'manipulative' is especially significant. It is and was virtually a term of art when used in connection with securities markets. It connotes intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities."

126. See *SEC v. Thermal Power Co.*, [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,265 (D.D.C. 1975).

127. See *supra* note 99.

128. *Green v. Santa Fe Indus., Inc.*, 533 F.2d 1283, 1304-07 (2d Cir. 1976).

independent, substantive right totally unrelated to the anti-fraud scheme of the federal securities laws and in complete derogation of a valid state rule regulating corporate activity. Indeed, the majority appears to have ignored the Supreme Court's decision in *Erie R. Co. v. Tompkins*, 304 U.S. 64 (1939), . . . which put an end to federal common law and forbade the federal courts from formulating their own "better rule".¹²⁹

Perhaps the result in *Marathon* can be justified since, absent a federal check, defensive actions by target management might as a practical matter go unregulated because of the applicability of the business judgment rule in actions predicated on state law.¹³⁰ Similar reasoning, however, was rejected by the Supreme Court in *Green*.¹³¹ Moreover, Judge Kinneary had held in *Marathon* that the business judgment rule did not apply, as a matter of law, and that, as a matter of fact, the defendant directors had affirmatively proven that the grant of the options was for a good faith business purpose and that the exercise price under each option was fair. Apparently, given the state law duty to resist an inadequate or illegal tender offer, actions undertaken in fulfillment of that duty should not be subject to challenge under the Williams Act provided that full disclosure has been made.¹³²

The *Marathon* manipulation theory could apply to virtually any tactic designed to aid one side or the other in a takeover battle. To be sure, the *Marathon* court noted that the stock option "was large enough in this takeover contest to serve as an artificial and significant deterrent,"¹³³ and *Marathon's* interest in the Yates Field was described as "a very important attraction to Mobil and other potential bidders for control of Mara-

129. *Id.* at 1304, 1307 (footnote omitted).

130. *See, e.g.,* *Panther v. Marshall Field & Co.*, 646 F.2d 271, 299 (7th Cir.) (Cudahy, J., concurring in part and dissenting in part) ("I emphatically disagree that the business judgment rule should clothe directors, battling blindly to fend off a threat to their control, with an almost irrebuttable presumption of sound business judgment, prevailing over everything but the elusive hobgoblins of fraud, bad faith or abuse of discretion."), *cert. denied*, 102 S. Ct. 658 (1981).

131. *See, e.g.,* Address of SEC Comm'r Sommer (Nov. 14, 1974), *reprinted in* [1974-1975 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,010.

132. The question of whether a breach of state law fiduciary duties can be turned into a disclosure violation (based upon a failure to disclose the alleged breach) has yet to be generally resolved under the federal securities laws. *But see supra* note 87. *Compare* *Goldberg v. Meridor*, 567 F.2d 209 (2d Cir. 1977), *with* *Bucher v. Shumway*, [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,142 (S.D.N.Y. 1979), *aff'd*, 622 F.2d 572 (2d Cir.), *cert. denied*, 449 U.S. 841 (1980). Federal and state concepts are not inherently exclusive, however, even under the securities laws. For example, in *State Teachers Retirement Bd. v. Fluor Corp.*, [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,340 (S.D.N.Y. 1980), *aff'd in part, rev'd in part on other grounds*, [1981 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,005 (2d Cir. 1981), the District Court for the Southern District of New York expressly held that the business judgment rule generally governs decisions as to the timing of disclosure to the investment community. Other courts have reached similar conclusions in rule 10b-5 cases. *E.g.,* *Financial Indus. Fund, Inc. v. McDonnell Douglas Corp.*, 474 F.2d 514, 518 (10th Cir.) (en banc), *cert. denied per curiam*, 414 U.S. 874 (1973). Thus, the complete divorce of federal and state concepts in *Marathon* appears to be inconsistent with other developments under the federal securities laws.

133. *Marathon*, 669 F.2d at 375.

thon."¹³⁴ However, the *Marathon* court's underlying rationale that the challenged options prevented all participants from "competing on a par"¹³⁵ has a much broader potential application.¹³⁶ While some Chicago-school economists have argued for a legal theory that prohibits all defensive actions other than mere disclosure,¹³⁷ the pre-*Marathon* law, properly so, was decidedly to the contrary.¹³⁸ Nonetheless, *Marathon* remains the law of the Sixth Circuit and, therefore, provides a basis for challenging many defensive and offensive actions given the almost limitless jurisdiction and venue provisions applicable to most nationwide tender offers.¹³⁹ Thus, the question becomes one of plumbing *Marathon's* conceptual limits.

III. TACTICS AND STRATEGIES AFTER *MARATHON*

A. Defensive Actions

Marathon has received an indifferent reception outside the Sixth Circuit. The first post-*Marathon* case involving a challenge to a defensive action was *Whittaker Corp. v. Edgar*.¹⁴⁰ In that case the bidder, Whittaker Corporation, sought to enjoin an asset sales agreement entered into by the subject company, Brunswick Corporation. The agreement provided for the swap of shares of Brunswick acquired pursuant to American's negotiated tender offer in exchange for Brunswick's crown jewel, the Sherwood Division. Judge Flaum, however, attempted to distinguish *Marathon* because *Whittaker* did not involve an option (even with the broad conditions in the controlling documents, some of which had already been triggered), and because the proposed sale of the crown jewel had not, in his view, created an artificial ceiling in the tender offer market for the acquisition of Brunswick.¹⁴¹ Finally, Judge Flaum held that "[a] sale of a substantial asset by a corporation in the face of a hostile tender offer standing alone is not a violation of section 14(e)."¹⁴²

Judge Flaum's efforts to distinguish *Marathon* do not withstand analysis. Whether a proposed asset or stock transaction is structured as an option or as a binding agreement is seemingly irrelevant to an analysis of its

134. *Id.*

135. *Id.*

136. The *Marathon* theory has already been employed in the context of an 8.8% block of stock (the stock option in *Marathon* was for slightly fewer than 18.5% of *Marathon's* shares). *Hanna Mining Co. v. Norcen Energy Resources, Ltd.*, No. C82-959 (N.D. Ohio June 11, 1982); see *infra* text accompanying notes 165-72.

137. See Easterbrook & Fischel, *The Proper Role of Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1 (1981); Easterbrook & Fischel, *Takeover Bids, Defensive Tactics and Shareholders' Welfare*, 36 BUS. LAW. 1733 (1981).

138. See *Panter v. Marshall Field & Co.*, 646 F.2d 271 (7th Cir.), cert. denied, 102 S. Ct. 658 (1981); see also Lipton, *Takeover Bids in the Target's Boardroom*, 35 BUS. LAW. 101 (1979); Lipton, *Takeover Bids in the Target's Boardroom; An Update After One Year*, 36 BUS. LAW. 1017 (1981).

139. See 15 U.S.C. § 78aa (1976).

140. [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,483 (N.D. Ill.), *aff'd mem.*, Nos. 1305 & 1307 (7th Cir. Mar. 5, 1982).

141. *Id.* at 92,832.

142. *Id.*

effect on the tender offer market or to a determination that all participants are prevented from "competing on a par" for control of the subject company.¹⁴³ Of course, Judge Flaum correctly noted that cases before *Marathon* had held that dispositions of assets and similar defensive measures, by themselves, did not violate section 14(e).¹⁴⁴ Perhaps the true distinguishing feature between *Whittaker* and *Marathon* is that the asset transaction in the former case was with an unaffiliated third person, while the asset option in *Marathon* was exercisable only in the event that another company gained control of the subject company. Under the circumstances, the asset option would never come into play if the ultimate purposes of the contracting parties were fulfilled. Still, the effect on bidders of the asset agreements in both *Whittaker* and *Marathon* was analytically identical, and the stock option in *Marathon*, held by itself to be manipulative by the Sixth Circuit, was immediately exercisable. Accordingly, a more plausible explanation of *Whittaker* is that it simply manifests Judge Flaum's discomfort with *Marathon*'s underlying rationale.

*Marshall Field & Co. v. Icahn*¹⁴⁵ was more overtly inconsistent with *Marathon*. Icahn, an approximately 30% holder (together with a section 13(d)(3) "group")¹⁴⁶ of the subject company, Marshall Field & Co., sued to enjoin enforcement of a stock option exercisable at the initial cash tender offer price (increased one day after the option was granted) of a two-step White Knight agreement between Marshall Field and BATUS, Inc. and a first-refusal right relating to Marshall Field's Chicago retail stores (its crown jewel). Judge Level, however, refused the 30% holder's application for relief against the allegedly lock-up options. While perfunctorily distinguishing *Marathon* (based principally upon a perceived failure to prove irreparable harm, viz., that any potential bidder had been deferred by the options), Judge Level's decision was ultimately grounded in a disagreement with the *Marathon* court's analysis:

I doubt that [*Marathon*] represents the law in this circuit. In my view the reasoning of that decision could unduly interfere with the right of company management to combat a takeover attempt that it believes in good faith to be harmful to its shareholders. In my view the securities laws do not bar management from taking action in the best interests of its shareholders even if this will make more difficult the success of a disfavored offeror. The rule might be otherwise on a showing that management is acting for its own interests in violation of its fiduciary duty to its shareholders. No such showing has been made here.¹⁴⁷

With respect to lock-up arrangements, stock options will probably be upheld after *Marathon* if, as in the *Icahn* case, they are structured at the

143. *Marathon*, 669 F.2d at 375-77.

144. E.g., *Missouri Portland Cement Co. v. Cargill, Inc.*, 498 F.2d 851 (2d Cir.), cert. denied, 419 U.S. 883 (1974); *Altman v. Knight*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,040 (S.D.N.Y.), amended, 431 F. Supp. 309 (S.D.N.Y. 1977); *Graphic Sciences, Inc. v. International Mogul Mines Ltd.*, 397 F. Supp. 112 (D.D.C. 1974); see *supra* text accompanying notes 67-80.

145. [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,616 (S.D.N.Y. 1982).

146. 15 U.S.C. § 78m(d)(3) (1976).

147. [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,616, at 93,061.

best price being offered in the marketplace.¹⁴⁸ Perhaps asset agreements can be structured as binding contracts (*Whittaker*), or as first-refusal rights (*Icahn*). While such structural approaches may be sufficient to bring the subject agreements within *Whittaker* and *Icahn*,¹⁴⁹ whether the facts in either case constitute a basis for a principled distinction of *Marathon* is unclear.

Whittaker and *Icahn* do indicate that *Marathon* may not find wide acceptance outside the Sixth Circuit, and courts within that circuit may attempt to confine its application. Perhaps the most obvious judicial avenue will be to limit *Marathon* to acts and transactions that have a major impact upon the balance between competing bidders or the bidder and subject company. Thus, the courts should normally permit previously upheld actions such as entering into long-term executive employment contracts,¹⁵⁰ changing the composition of the subject company's board of directors,¹⁵¹ increasing dividends,¹⁵² repurchasing stock,¹⁵³ or entering into defensive litigation.¹⁵⁴ The ultimate effect of *Marathon*, however, on defensive actions such as corporate liquidations¹⁵⁵ or asset or stock transactions that do not fit within the holdings of *Whittaker* or *Icahn* is presently impossible to divine.

B. Marathon as the Predicate for Defensive Litigation

Although *Marathon* involved an action by a competing bidder, the decision presents very significant opportunities for litigation initiated by the subject company that challenges actions by the bidder. Because of its emphasis upon the "effect on the market" of tender offer conduct, the impact of *Marathon* in this setting has already been felt.¹⁵⁶ In the typical Williams Act case injunctive relief is normally limited to an offer prohibiting future purchases or a tender offer pending the filing and dissemination of an accurate SEC disclosure document.¹⁵⁷ Exceptions to the normal rule exist,

148. The stock option in *Marathon* was priced at a level that approximated the then present value of the securities offered in the second step of U.S. Steel's takeover offer. Price escalator provisions (perhaps only up to specified price levels), while removing some of the economic motivation for stock lock-ups, would enhance the likelihood of this result.

149. The *Marathon* court expressly disclaimed any intention to formulate a broad rule of law applicable to all stock and asset options in this context, 669 F.2d at 374, thereby implicitly suggesting that some analogous actions may pass muster even in the Sixth Circuit.

150. See *Missouri Portland Cement Co. v. Cargill, Inc.*, 498 F.2d 851 (2d Cir.), cert. denied, 419 U.S. 883 (1974).

151. See *Graphic Sciences, Inc. v. International Mogul Mines Ltd.*, 397 F. Supp. 112 (D.D.C. 1974).

152. See *Humana, Inc. v. American Medicorp, Inc.*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,286 (S.D.N.Y. 1978).

153. See *Herald Co. v. Seawell*, 472 F.2d 1081 (10th Cir. 1972). But see *Orbanco, Inc. v. Security Bank*, 371 F. Supp. 125 (D. Ore. 1974).

154. See *Panther v. Marshall Field & Co.*, 646 F.2d 271 (7th Cir. 1981).

155. See *Joseph E. Seagram & Sons v. Abrams*, 510 F. Supp. 860 (S.D.N.Y.) (threatened liquidation of target company enjoined).

156. *Hanna Mining Co. v. Norcen Energy Resources Ltd.*, No. C82-959 (N.D. Ohio June 11, 1982).

157. E.g., *Treadway Cos. v. Care Corp.*, 638 F.2d 357, 380 (2d Cir. 1980); *Chromalloy Am. Corp. v. Sun Chem. Corp.*, 611 F.2d 240, 249 (8th Cir. 1979); *General Aircraft Corp. v.*

however, particularly when the defendant's conduct is willful or gives it a significant advantage over the target or competing bidders. For example, in *General Steel Industries, Inc. v. Walco National Corp.*¹⁵⁸ the District Court for the Eastern District of Missouri ordered the rescission of shares purchased by a bidder in open-market transactions prior to the commencement of its tender offer under a schedule 13D filing that falsely represented the open-market purchases as merely for investment purposes. The *General Steel* court reasoned:

(i) Walco's illegally obtained blocking position has placed it in a position to inhibit competing offers and has made it extremely difficult for GSI to arrange for a merger, business combination or to pursue other possible business opportunities which would be favorable to *all* GSI shareholders (as opposed to the 19 percent which Walco seeks). Once Walco controls GSI, it will have little, if any, incentive to pay a premium to the remaining GSI shareholders in a subsequent merger of GSI and Walco. In addition, Walco's acquisition of over 51% of GSI will reduce the liquidity of GSI stock held by the remaining GSI shareholders.

...
(iii) Shareholders who sold to Walco irretrievably lost their ability to obtain a control premium for their shares—a loss not compensable by a monetary award—and unwittingly sacrificed their right to knowingly determine who should be in a position to control GSI.¹⁵⁹

Walco appealed the trial court's ruling to the Court of Appeals for the Eighth Circuit, but the case was settled prior to a decision by the appellate court. While the appeal was pending, the SEC filed an amicus curiae brief supporting the decision of the trial court,¹⁶⁰ the contents of which it described as follows:

The Commission urged in its brief that the district court's equitable jurisdiction to remedy Section 13(d) violations includes the authority to order any relief appropriate under the circumstances. The Commission expressed the view that equitable remedies in addition to corrective disclosure, such as rescission and divestiture, may be necessary or appropriate to remedy violations of the Williams Act, particularly in cases where the defendant deliberately violated Section 13(d) and the illegal conduct had permitted the defendant to obtain a sufficient number of shares to inhibit competing tender offers or merger proposals. In such cases, absent rescission or divestiture or other remedy removing the wrongfully obtained blocking position, shareholders could be irreparably harmed and the defendant would be permitted to benefit from its wrongful conduct.¹⁶¹

Lampert, 556 F.2d 90, 97 (1st Cir. 1977); *Raybestos-Manhattan, Inc. v. Hi-Shear Indus., Inc.*, 503 F. Supp. 1122 (S.D.N.Y. 1980); *Standard Metals Corp. v. Tomlin*, 503 F. Supp. 586 (S.D.N.Y. 1980); *Avnet, Inc. v. Scope Indus.*, 499 F. Supp. 1121 (S.D.N.Y. 1980); *Brascan Ltd. v. Edper Equities Ltd.*, 477 F. Supp. 773 (S.D.N.Y. 1979).

158. [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,402 (E.D. Mo. 1981).

159. *Id.* at 92,418.

160. SEC Securities Litigation Release No. 9533 (Dec. 21, 1981), [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,387.

161. *Id.* at 92,344.

General Steel did not represent a radical departure from prior law¹⁶² given that the relief ordered related only to shares purchased following the filing of a false Williams Act disclosure document.

Marathon presents a fertile basis for extending the law well beyond the result reached in cases such as *General Steel* precisely because the *Marathon* court expressly rejected the contention that nondisclosure or deception is an essential element of section 14(e) manipulation.¹⁶³ In light of *Marathon's* emphasis on whether the challenged conduct prevents other tender offer participants from "competing on a par"¹⁶⁴ for control of the subject company, curative disclosure, the elixir usually proffered by a bidder found to have violated the Williams Act, will simply be irrelevant in many cases.

This point was graphically illustrated in *Hanna Mining Co. v. Norcen Energy Resources Ltd.*¹⁶⁵ In *Hanna Mining* the bidder, Norcen Energy Resources Limited, had previously amassed through open-market purchases an 8.8% block of stock of the target, The Hanna Mining Company, prior to making a schedule 13D filing in which it represented the purpose of its purchases as mere investment. Five months later Norcen publicly announced its intention to make a tender offer for control of Hanna. On the date of the public announcement, Hanna obtained a temporary restraining order based upon alleged violations of section 10(b),¹⁶⁶ 13(d), 14(e), and 20(a)¹⁶⁷ of the Securities Exchange Act. The gravamen of Hanna's complaint was that Norcen had misrepresented the purpose of its stock acquisitions in its schedule 13D filing to enable it initially to purchase the 8.8% block¹⁶⁸ and to permit it to make its subsequent tender

162. See, e.g., *Mosinee Paper Corp. v. Rondeau*, 500 F.2d 1011, 1017 (7th Cir. 1974) (injunction against voting shares acquired in violation of § 13(d) for 5 years); *rev'd on other grounds*, 422 U.S. 49 (1975); *Ronson Corp. v. Liquifin A.G.*, 483 F.2d 846 (3d Cir. 1973) (affirming preliminary injunction, inter alia, disenfranchising defendant who acquired shares in violation of § 14(e)), *cert. denied*, 419 U.S. 870 (1974); *Twin Fair, Inc. v. Reger*, 394 F. Supp. 156, 161 (W.D.N.Y. 1975) (preliminary injunction against, inter alia, voting any shares acquired in violation of § 13(d)).

163. See *supra* text accompanying notes 110-13.

164. *Mobil Corp. v. Marathon Oil Co.*, 669 F.2d 366, 378 (6th Cir. 1981).

165. No. C82-959 (N.D. Ohio June 11, 1982).

166. 15 U.S.C. § 78j(b) (1976).

167. *Id.* § 78t(a).

168. With respect to the schedule 13D issue, Hanna argued in the Sixth Circuit (the appeal was dismissed on July 7, 1982, after settlement of the litigation between the parties):

[W]ithout its false statement of mere passive investment intent, Norcen would have been unable to buy the 580,000-share block offered to it on October 28, 1981 in the first place because of the premerger notification requirements of the [Hart-Scott-Rodino Antitrust Improvements Act of 1976. 15 U.S.C. §§ 18a, *et seq.* (1976) (the "H-S-R Act").] The filing and minimum 30-day waiting period requirements of the H-S-R Act do not apply to acquisitions of less than 10% of a company's stock if such acquisitions are solely for "investment" purposes. 16 C.F.R. § 802.9. Thus, in order to buy the block that gave rise to its disclosure obligations under Section 13(d), Norcen *had to lie* about its ultimate purpose. Judge Manos dismissed plaintiffs' separate claim under the H-S-R Act on the ground that plaintiffs lacked standing to assert that claim. Plaintiffs believe that such dismissal was erroneous, and have appealed it. However, without respect to the outcome of the issue of whether plaintiffs have standing to assert a claim under the H-S-R Act, the fact remains that

offer at an artificially low price and with a minimum risk of competition.

Following a seven-day hearing, Judge Manos granted Hanna's motion for a preliminary injunction. With respect to Hanna's section 13(d) claim, Judge Manos essentially relied upon *General Steel*.¹⁶⁹ With respect to the

evasion of the requirements of that Act (which defendants have never disclaimed) was undoubtedly one of the principal motives for the false statements in Norcen's Schedule 13D.

Brief of Appellees The Hanna Mining Co., Carl E. Nickels, and John Gurgle at 16 n.17, *Hanna Mining Co. v. Norcen Energy Resources Ltd.*, No. C82-959 (N.D. Ohio June 11, 1982).

Nonetheless, the Norcen defendants argued that the market purchases were not "in connection with" a tender offer and therefore not actionable under § 14(e). Judge Manos found, however:

Contrary to the defendants' contention that Norcen's intent to make a tender offer for Hanna was formulated on the eve of the tender offer, this court finds that the evidence *establishes conclusively* that Norcen contemplated such action as early as the date on which it filed its Schedule 13D if not earlier.

Hanna Mining Co. v. Norcen Energy Resources Ltd., No. C82-959, at 39 (N.D. Ohio June 11, 1982) (emphasis in original). In *O'Connor & Assocs. v. Dean Witter Reynolds*, 529 F. Supp. 1179 (S.D.N.Y. 1981), the argument that section 14(e) can apply only after public announcement of a tender offer was expressly rejected. The *O'Connor* court upheld rule 14c-3, 17 C.F.R. § 240.14c-3 (1981), which was promulgated under section 14(e), governing insider trading on tender offer knowledge from the point at which "any person has taken a substantial step or steps to commence . . . a tender offer." Going to the heart of the interests that the Williams Act was intended to protect, the *O'Connor* court reasoned:

It is true that here the allegedly fraudulent conduct occurred prior to the announcement of the tender offer proposal. However, this circumstance does not change the fact that the alleged failure to disclose the impending announcement of the tender offer proposal worked to deny the target invest[or] the relevant information on which to decide whether to sell his shares in the same manner as fraudulent conduct operates when an offer has already been publicly announced.

529 F. Supp. at 1191. The *O'Connor* court concluded that any other reading would present "the risk of 'defeating in substantial part the very purpose of the Act.'" *Id.*; see also *Lewis v. McGraw*, 619 F.2d 192, 195 (2d Cir.), ("[I]njunctive relief . . . may be available [under section 14(e)] to restrain or correct misleading statements made during the period preceding a tender offer where it appears that such an offer is likely, and that reliance upon the statements at issue is probable under the circumstances."), *cert. denied*, 449 U.S. 951 (1980); *Berman v. Gerber Prods. Co.*, 454 F. Supp. 1310, 1318 (W.D. Mich. 1978); *Applied Digital Data Sys. Inc. v. Milgo Elec. Corp.*, 425 F. Supp. 1145, 1152, 1154-55 (S.D.N.Y. 1977); *E. ARANOW & H. EINHORN*, *supra* note 18, at 121-25; *A. FLEISCHER*, *supra* note 26, at 69-70.

In *Hanna* the trial court found that all of Norcen's activities were directed toward its contemplated tender offer. The nexus, therefore, between the alleged fraud and the tender offer was enough to fall within the broad substantive reach of the "in connection with" requirement. See, e.g., *Superintendent of Ins. v. Bankers Life & Casualty Co.*, 404 U.S. 6, 12-13 (1971) (interpreting "in connection with" language of rule 10b-5 to reach "deceptive practices touching [the] sale of securities"); *Bolton v. Gramlich*, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,438, at 92,593 (S.D.N.Y. Jan. 28, 1982) ("In deciding whether the harm to the [plaintiff] occurred in connection with the purchase or sale of securities, the Court declines to erect partitions around these closely connected transactions." (footnotes omitted)).

169. Judge Manos concluded:

Similar to the irreparable harm found in [*General Steel*], this court finds that the evidence establishes that: (1) by reason of its 8.8 percent interest, Norcen has a competitive advantage over any other potential offeror for Hanna; (2) once Norcen controlled Hanna, Norcen would have no incentive to pay a premium to the remaining Hanna shareholders in the event of a subsequent merger of the two companies and, therefore, the remaining shareholders would possess an illiquid investment; and (3) the Hanna shareholders who sold shares on the open market during the period Norcen's original Schedule

Hanna plaintiffs' section 14(e) claim, Judge Manos found:

Here, the evidence establishes that Norcen's representation of an investment intent in the acquisition of its 8.8 percent interest in Hanna had an effect on the price of Hanna stock which the defendants' expert conceded was trading [immediately prior to the tender offer announcement] at a price lower than it would have been had Norcen disclosed its intent to acquire control. The effect Norcen's misrepresentations had on the price for Hanna stock also made it appear that the tender offer price of \$45.00 per share, which Norcen announced on April 5, 1982, was a substantial premium over what the evidence establishes was a market price effected by "means unrelated to the natural forces of supply or demand." [*Mobil Corp. v. Marathon Oil Co.*, 669 F.2d 366, 374 (6th Cir. 1981).] The evidence thus supports the plaintiffs' contention that Norcen's repeated misrepresentations of its intention to acquire control of Hanna and the [block purchase] of Hanna stock on October 28, 1981 were manipulative violations of section 10(b), Rule 10b-5 and section 14(e).¹⁷⁰

Relying upon the fact that the Sixth Circuit in *Marathon* had specifically rejected the contention that misrepresentation or deception were essential elements of section 14(e) manipulation,¹⁷¹ Judge Manos held that curative disclosure was not enough to remedy the manipulation that had been shown in the preliminary injunction hearing.¹⁷² Accordingly, Judge Ma-

13D was in effect irretrievably lost their ability to obtain a control premium, a loss not compensable by a monetary award.

Hanna Mining Co. v. Norcen Energy Resources Ltd., No. C82-959, at 42-43 (N.D. Ohio June 11, 1982).

170. *Id.* at 50.

171. *Id.* at 49.

172. The defendants' third and final contention is that even if they engaged in a manipulative scheme, the proper remedy is to eliminate the manipulation by ordering corrective disclosure and then permit the tender offer to proceed. Although the remedy urged by the defendants may be proper in some circumstances, it is utterly without merit in this case.

Although formulation of an appropriate remedy must await final hearing on a permanent injunction, the evidence presented by the plaintiffs on their motion for a preliminary injunction supports the remedy of divestiture that they request. The evidence establishes that by reason of the large block of stock acquired by Norcen on October 28, 1981, Norcen has an advantage over any other potential offeror for Hanna.

Indeed, if, as in this case, the evidence indicates a continuing fraud, divestiture of the stock acquired in the transaction which gave rise to the statutory duty violated in a false Schedule 13D filing seems as appropriate a remedy as the divestiture ordered in *General Steel Industries* of the stock purchased after the false Schedule 13D was filed. Any different result would mean that an acquiring corporation could engage in the most deliberate form of misrepresentation in its statutory filings and when its fraud is discovered merely file corrective amendments and keep the benefits of its wrongful conduct regardless of how that conduct may continue to injure shareholders of the corporation whose stock it has acquired.

Id. at 50-52. As in *General Steel*, the SEC submitted an amicus curiae brief in *Hanna* and asserted that district courts have the power to grant injunctive relief that extends beyond mere corrective disclosure:

To the extent . . . that defendants . . . suggest that the remedies available to the district court were restricted to corrective disclosure as a matter of law, the

nos issued a preliminary injunction prohibiting the Norcen defendants from proceeding with their offer pending a trial on the merits unless the 8.8% block of Hanna stock was disposed of pursuant to a court-supervised plan and other appropriate remedial steps were taken.

Without *Marathon*, whether the relief ordered in *Hanna* would have been appropriate is doubtful. Even after *General Steel* (itself seemingly influenced by the arguments advanced in *Marathon*), a finding of a violation of section 13(d) would not necessarily be sufficiently related to a proposed tender offer to justify injunctive relief against the offer without the "effect on the market" analysis that constitutes *Marathon*'s theoretical underpinning. *Marathon* formed the basis, however, for Judge Manos's emphasis in *Hanna* upon the effect of Norcen's prior disclosures on the market (making the offered premium look substantial) and on the possibility of competitive bidding. Thus, the relief ordered in *Hanna* was appropriate.

IV. CONCLUSION

After *Marathon* an inherent risk arises in the previously traditional tactic of taking a position in a potential target company through open-market purchases in order to average-down the cost of an entire acquisition. The negotiated purchase of a large block of stock may also be vulnerable to challenge if a reasonable nexus between the purchase and a Williams Act violation or a subsequent takeover bid can be established. On the other hand, *Marathon* provides the basis for challenging many traditional defensive reactions. Thus, *Marathon*, in the context of the demise of state takeover legislation, the SEC's 1979 tender offer rules, and the subject company's affirmative duty to resist an inadequate or illegal takeover bid, may well portend an era of surprise offers with the toe-to-toe battles being fought out in the courts. Not at all clear, however, is whether shareholder interests will necessarily be served by this conduct.

Commission disagrees. There is an important distinction between the *propriety* of, and the *power* to grant, equitable relief, and, in this suit based on Williams Act violations, the district court had broad equitable powers. Regardless of whether the relief granted here was *appropriate* under all the circumstances, that equitable remedy was, in the Commission's view, one of the "variety of tools," in addition to corrective disclosure, which the court had the *power* to order.

Memorandum of the SEC, Amicus Curiae, at 22 (emphasis in original), *Hanna Mining Co. v. Norcen Energy Resources Ltd.*, No. 3386 (6th Cir.), *dismissed by stipulation*, No. 3386 (6th Cir. July 7, 1982).