May 9, 1983

Preliminary Report of The Subcommittee Dealing with the Interrelationship of Various Regulatory Schemes

The Subcommittee recommends that the Committee limit its review of the interrelationship of various regulatory schemes to considering whether, in general, these regulatory schemes are or should be coordinated procedurally with the rules relating to changes of control.

Irwin Schneiderman, Jeffrey Bartell and Frank Easterbrook of the Subcommittee, as well as John Spurdle of the Committee, Chairman Shad and members of the SEC staff met with Chairman Miller of the Federal Trade Commission and members of his staff to review the compatibility of procedural requirements for Hart-Scott-Rodino filings with Williams Act time periods. Presently, a cash tender offer involves an initial fifteen day Hart-Scott-Rodino waiting period while a securities tender offer involves an initial thirty day waiting period. It was agreed that the cash-securities dichotomy made no sense and that the test should be whether the offer was hostile or friendly. Chairman Miller and his staff stated that the dichotomy could be eliminated under the FTC's present rules which permit them to shorten waiting

periods. It was also suggested to Chairman Miller and his staff that if the Williams Act time period had expired but the Hart-Scott-Rodino period had not, a bidder should be allowed at his own risk to purchase the shares provided they were held separate, to be disposed of in the event an antitrust violation was established. Chairman Miller indicated that authority existed to shorten the Hart-Scott-Rodino waiting period in exchange for a hold separate agreement.

We believe the Committee should not consider substantive issues with respect to tax, banking, antitrust or ERISA law or policy. These are matters outside the area of the Committee's expertise, and beyond the statutory responsibility of the Securities and Exchange Commission (SEC) by which the Committee was appointed.

The group referred to above also met with Robert G. Woodward, Acting Tax Legislative Counsel, U.S. Department of Treasury, and Federal Reserve Chairman Volcker to review tax and banking matters. The conclusion that the Committee should not consider substantive issues in these areas was reenforced by these meetings.

With respect to tax matters, the Pandora's box that would be opened by recommending a tax carry forward basis in change of control situations became evident. In one limited area Mr. Woodward indicated that the Treasury Department might be receptive to a change. When stock and cash are now issued pro rata to shareholders of a target, there is a risk that the cash will be taxed as a dividend rather than as a capital gain. To avoid this, a very complicated election procedure has been developed. Mr. Woodward agreed that this made no particular sense and undertook to give the matter consideration.

Chairman Volcker was asked about the statement attributed to him by the Senate Banking Committee that take-overs distorted banking judgment and credit markets. Chairman Volcker stated that while his staff believed that take-overs had no effect on credit markets, he would say merely that any effect had been exaggerated. He stated that whatever effect there was did not warrant anything such as allocation of credit by the Federal Reserve. He expressed concern that some transactions moved ahead so quickly that credit judgments might have been distorted. He also expressed concern about the use of short term borrowing to retire equity. When told that the Committee was considering putting equity offers on a par with cash offers he expressed support for this as a way of solving the problems referred to above.

With respect to the proper relationship of federal and state securities and corporate laws, the Committee appears, preliminarily, to favor a regime of neutral regulation, in which the interests of the shareholders of bidders and targets are protected. This is the current policy expressed in the Williams Act. The Supreme Court of the United States in Edgar v. Mite, which struck down the Illinois Take-over Act on the ground that it imposed an excessive burden on interstate commerce, referred to the Congressional policy underlying the Williams Act by saying:

> "Congress sought to protect the investor not only by furnishing him with the necessary information but also by withholding from management or the bidder any undue advantage that could frustrate the exercise of an informed choice."

The Court recognized that some state regulation in the area is permissible. Permissible regulation would, of course, have to be compatible with Congressional policy and be confined to matters of substantial local interest.

The North American Securities Administrators Association has submitted a proposed statement indicating that if certain perceived abuses in connection with tender

offer contests are curtailed, the resurrection of state take-over statutes will not be their primary focus. The Subcommittees on Regulation of Bidders and Regulation of Target Companies should carefully consider the points raised by NASAA.

If certain tactics engaged in by bidders or by targets, such as those discussed by NASAA, are considered by the Committee to violate the objectives of neutrality and protection of shareholders, the SEC would appear to have adequate authority under the Williams Act to regulate such activities. See Mobil Corp. v. Marathon Oil Co., CCH Fed.Sec.L.Rep. ¶ 98399 (6th Cir. 1981). State corporation statutes may also be employed to provide certain remedies in this area.

The Subcommittee has noted that many corporations now are seeking shareholder approval of shark repellent provisions in their charters and that many have obtained such approvals in the past. Shark repellents are permissible under state law. If the Committee concludes that certain shark repellents have undesirable effects in view of the objectives of tender offer regulation, the Committee should consider whether periodic reapproval of such matters by shareholders should be required with full disclosure under the proxy rules of the economic and other

effects of the approval of such provisions. The Committee should also consider what vote should be required to approve or reapprove such charter provisions, e.g., should a super-majority requirement with respect to mergers require a super-majority approval at the outset? Other such aspects of corporate governance under the state corporation statutes in a tender offer context are appropriate topics for Committee review.

Laws applicable to regulated industries, such as insurance, banking, transportation and communications, present separate policy considerations. Although the Subcommittee does not believe the Williams Act should preempt or supersede the laws (state or federal) in such areas, regulation of companies in these industries should be procedurally compatible with the Williams Act wherever possible. For instance, even though regulatory approval of a change of control may be required, a tender offer to effect such change of control should be allowed to proceed, with consummation being conditioned on receipt of necessary approvals.

In summary, the Subcommittee believes that whatever amendments to the 1934 Act and rules thereunder are proposed to improve shareholder protection in tender

offers, those amendments should disrupt as little as possible the various other regulatory schemes applicable to parties to a tender offer. If in the Committee's view state corporate law can provide a fair procedure for tender offers and other changes of corporate control which is not incompatible with the Williams Act, the Committee should not hesitate to recommend a dual regime of regulation.

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