LUISS

Department of Economics and Finance

Chair of Law and Economics (Business and Corporate Law; Antitrust and Regulation)

PAST, PRESENT, AND FUTURE OF POISON PILLS

Prof. Pierluigi Matera

SUPERVISOR

Riccardo De Marcis

CANDIDATE

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To my cherished grandparents

To my supportive parents

To my charming Giulia

To Francesco and Gabriele

To my Italian family

To my American family

To my family at Libra Legal Partners

Abstract

The recent COVID-19 pandemic and related stock market crash led many U.S. companies to adopt shareholder rights plans – well-known defensive tactics, originated to contrast the 1980s takeover wave, which have resisted the passing of time and, despite evolved, still proved effective.

The number of plans deployed at the outbreak of the pandemic was exorbitant: in the first quarter of 2020, the number of active poison pills increased fivefold from the previous 3-year period. Nevertheless, as the economy recovered from the shock, a downward trend followed, settling the plans' adoptions at pre-pandemic levels.

Considered the unprecedented crisis, boards either abided by the predetermined standard or ventured into atypical provisions hoping that courts would benevolently accept their plans. Most notably, in the Williams *case, both the Delaware Chancery and Supreme Court ultimately barred directors from deploying an aggressive defensive measure, in spite of the emergency conditions, by rigidly applying the predetermined standard of judicial review. However, the ruling introduced some novelty as it concentrated mostly on the "proportionality" test rather than on "reasonableness", which to a broader extent may lead to speculate a tacit acceptance of the first* Unocal *prong is entailed in specific situations.*

Consistently, it can be inferred that boards cautiously adopting said defence can at the same time apport benefits to the corporation (share price boost), equity owners (higher deal price should an acquisition go forward, maximisation of shareholder value and share purchase at discount,) and themselves (an augmented negotiating power, and an increased amount of time to value the offer).

Therefore, the decision in Williams*, by underlining the considerable benefits a plan may apport, on one side re-established the consolidated standard, but on the other side, it left the door ajar for future developments of the pill.*

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I. INTRODUCTION

Takeovers are at the same time the mechanism to enlarge and develop surviving businesses and regulate the market for corporate control. In fact, if on one side they are deemed to create value for companies and shareholders, they also serve as a regulatory system for directors in underperforming firms. Despite acquisitions may occur at any time throughout a company's life, it is proven takeover activity rises when the market is in ferment and prices are depressed, as bidders attempt to take control at bargain. The COVID-19 pandemic has clearly presented such opportunities.

It is common knowledge that new majority owners replace management once they obtain control; therefore, the latter deploys defensive tactics to remain in charge. Amongst the vast arsenal boards can choose from, a specific takeover defence returned to vogue consequently to

COVID-related market disruption: the shareholder rights plan – also known as poison pill. The number of companies adopting the said defence skyrocketed. At the end of 2019, amongst the S&P 1500, 25 had a poison pill in place while, just in one month – April 2020 –, 28 firms adopted shareholder rights plans[1].

They were first introduced during the golden age of M&A, the 1980s takeover wave, by Martin Lipton. Then, they were extensively used as they proved effective in thwarting off hostile bids. And later got disposed of due to adverse courts' decisions and opposing proxy advisors' opinions. The demise logically followed because on one side courts pre-empted, or at least hindered, boards from adopting shareholder rights plans by setting a stringent standard to justify a poison pill and, on the other side, firms such as ISS and Glass Lewis recommended to vote against directors deploying the said defence. However, following the share price depression caused by the pandemic, they rose from the ashes. Therefore, it is fair to ask why boards looked back at this quite dated defensive tactic; and the logical explanation is that the benefits are numerous and consistent. On directors' side, they augment the bargaining power by delaying the acquisition process and consequently allow shareholders' fiduciaries to negotiate a higher price. Moreover, they pump up the share price, dilute the acquirer's equity, and can even impair its financial stability through a flip-over provision that allows target stockholders to purchase the acquirer's company shares. Finally, target shareholders benefit from the plan as they are entitled to exercise a call option to purchase shares at discount.

Despite these enticing characteristics, a major problem frequently stems from poison pills: board entrenchment. Directors are accustomed to turn the defensive tactic to their own advantage by staggering themselves and avoiding being replaced rather than serving the shareholder value. Moreover, poison pills may even slow company's growth in the long run; in fact, downsides outweigh benefits, if not redeemed once the threat ends.

Considered the potentially damaging effects a pill may entail, courts have extensively ruled over the subject, and the long list of legal precedents boils down to the widely accepted *Unocal* standard: a two-prong test requiring directors to prove the reasonableness of the threat and the proportionality of the response in order for a court to uphold a poison pill. The standard was introduced in 1985 and has been the discrimen between approval or injunction ever since.

The standard has been applied to a wide variety of cases and courts have relied on it to rule in takeovers; however, given the unconventional traits of this pandemic crisis (prices dropped because of government restrictions rather than company or industry shocks), a

[1] *See infra* note 60.

question rapidly saw the light of the day: "Should boards be allowed to opt for unconventional defences? And if so, to what extent?". Managers took sides and they either adhered to the consolidated standard or deployed unprecedented anti-takeover mechanisms. In 2021, the Delaware Chancery Court provided an answer to the said dilemma in a decision regarding the Williams Company Inc.[2] later affirmed by the Supreme Court[3] en banc.

The Court's opinion seems to prevent any excessively daring poison pill, but it may have left the door ajar to an adjustment of the standard as the Court noted that a reasonable threat to swiftly accumulate 5 % of the shares without disclosure – in compliance with the federal regulation – was present. Commentators therefore speculated whether a more lenient standard will be applied in subsequent decisions and over the adaptive response lawyers will choose.

Consistently with the Chancery Court's decision, this paper argues that the standard of review is far from being changed, and directors shall be cautious in deploying an appropriate defensive mechanism, since an unconventional pill is unlikely to pass judicial scrutiny and will be enjoined. It further opines there is a tacit acceptance that a reasonable threat to the company is present under emergency conditions, but given the conjunctive nature of the test, poison pills need to comply with the long-established *Unocal* standard so not to be enjoined.

In Part II, firstly I explain the effects the pandemic has had on the market for corporate control and the divergencies from comparable crises – *i.e.*, the Spanish Flu and the 2008 financial crisis. Then, I sustain that, albeit the market returned quickly to its pre-pandemic level, board's intervention was necessary in light of the liquidity crisis originated and the consequent higher level of exposure to hostile takeovers. Further, the analysis continues on the main conflicts of interest arising in a takeover context which originate from the evergreen principal-agent problem and the diverging interests of majority and minority shareholders. In fact, a takeover may lead directors to act in their own interest rather than the shareholders' – which are commonly concerned mainly about the quick profit from the share premium they receive. However, the consideration received may also be a source of conflict amongst shareholders as it is not certain they will equally benefit from the transaction.

In section II B, the analysis further deepens to address the main implications, risks and rewards of a takeover and the discussion flows to the main statutes regulating tender offers, a common acquisition mechanism. A broad overview of the federal rules that bidders need to abide by when increasing their equity stake is present to fully grasp the threats suffered and the

[2] *The Williams Companies Stockholder Litigation*, Consol. C.A. No. 2020-0707-KSJM (Del. Ch. 2021).
[3] *Wolosky v. The Williams Companies Inc.,* Docket No. 139, 2021 (Del. 2021).

consequent boards' responses. Then, I investigate the four sustaining arguments to deploy a shareholder rights plan which are avoiding inefficient acquisitions, augmenting board's bargaining power, allowing directors to pursue the long-term strategy regardless of the temporary share price, and reserving the board some time to carefully assess the benefits and downsides of an acquisition.

Before delving into the peculiarities of the specific shareholder rights plans, I also introduce a second type of defensive tactic which is commonly used in conjunction with a poison pill: the staggered board. I point out the advantages a mix of the two brings to the corporation because, while a plan may be vulnerable if the bidder replaces management and redeems it, a staggered board will delay the acquisition process quite a lot, constraining the acquirer to win two consequent board elections to obtain control.

Part II ends with a punctual taxonomy of the features plans may entail, ranging from the mandatory trigger threshold and definition of beneficial ownership to the ad hoc provisions. Firstly, I present the prototypes of poison pills and the classical flip-over provision. Secondly, I signal how lawyers introduced the flip-in feature to block bidders from preventing white knights to save the target company. Finally, I scrutinise the most ingenious clauses; specifically the AIC, the redemption and the qualifying offer provision, the grandfather clause and even the back-end plan. To conclude, I report the two opposing views on the application of a pill – notably the entrenchment and the shareholder's interest view – and the peculiar finding that the effect on company's performance depends on the firm's age: the older it is, the worst are the downsides.

Part III, instead, enlarges upon the seminal decisions that have shaped jurisprudence in a chronological order. The first section reports the *Pogostin* decision – where the Court affirmed the business judgment rule as the proper standard of review – and further deepens on the milestones *Unocal, Moran* and *Revlon.* Namely, the first specified that directors are empowered to protect the corporate enterprise from threats and clarified a Court will not second-guess a business decision, so long as it can be attributable to a rational business process. Furthermore, it is well-known for its two-prong standard that has ruled over shareholder rights plans ever since. Then I present the *Moran* case, the first where a pre-bid poison pill was upheld. What stems from it is the concept of "preclusive" measure; the Court in fact noted it will not scrutinise boards' decision, if not preclusive. To conclude the reconnaissance of key decisions, the paper presents the *Revlon* decision and its principle to maximise share price.

In the following section, the paper moves towards the end of the 1980s and early 1990s analysing the contrasting *Paramount* decisions and the 1995 opinion in *Unitrin.* Further, it

reports three seminal cases of the 21st Century: *Selectica, Airgas,* and *Third Point.* The first treated an NOL pill (a special provision with a 5 % trigger). The second addressed the dilemma of the delegation of corporate powers from shareholders to directors; it gave an answer to the question whether a fully informed board acting in good faith, once a reasonable threat has been identified and employing a reasonable defensive tactic, can prevent stockholders from taking their own decision, and clarified directors are not empowered to reject any type of hostile bid. Finally, the third confirmed the applicability of the *Unocal* standard and upheld the pill as plaintiffs failed to demonstrate the board has rendered the proxy contest unattainable.

In Part IV, the paper reports the final answer Delaware Chancery Court gave to unconventional poison pills. It first presents the debated atypical poison pill in emergency conditions, then it reports three companies deploying a conventional pill to highlight the difference with the Williams company. Finally, it analyses the *Williams* decision inquiring into the key characteristics, and the court's scrutiny of the unconventional plan. In particular, it focuses on the implications this opinion entails as it both barred future pills from being upheld, while leaving the door ajar for a tacit acceptance of the first prong in an emergency scenario.

I conclude sustaining that, in wake of their flexibility and adaptiveness, poison pills can be extended to a wide variety of purposes and, so long as they abide by the firmly established standard, they may be used to fend off hostile bids as well as to curb activism.

II. RESPONDING TO A HOSTILE TAKEOVER: BOARD'S RESPONSES

A. *The COVID- 19 pandemic impacts on the market for corporate control*

March 2020 represented a twisting point for economic growth. In fact, as the World Health Organization (WHO) officially declared the outbreak of the COVID-19 pandemic[4], financial markets reacted and stock value sharply plummeted[5]. Investors panicked, and started selling their holdings, thereby draining out additional resources from the capital markets. This unprecedented stock crash, however, was quite different from the previous ones. As an example, the virus' nature is comparable to the 2003 SARS CoV-1, but the price drop was

[4] J. Ducharme, *World Health Organization Declares COVID-19 a 'Pandemic.' Here's What That Means* (2020), *Time*, https://time.com/5791661/who-coronavirus-pandemic-declaration/.

[5] *See* Scott R. Baker et al., *The Unprecedented Stock Market Impact of Covid-19* (2020), NBER working paper no. 26945, https://www.nber.org/system/files/working_papers/w26945 for the most relevant data on stocks performances.

greater in magnitude; or the sudden shock was comparable to the 2008 crisis, but the causes are distinct.

Although it is not an easy task to choose the right benchmark to comparatively assess the harshness of the 2019 pandemic, it is crucial so to have a general understanding of its detrimental impact. Firstly, with respect to its precursor SARS CoV-1, the COVID-19 pandemic caused a much deeper depression in the companies' value, and its effects reverberated on financial markets for more than a year[6]. Secondly, with respect to another thoroughly documented pandemic, the Spanish Flu, this time the virus's economic impact on was far greater, as the 20th Century shock was almost undetected by capital markets, despite its detrimental effect on world population. Finally, its impact on financial markets was comparable to the credit default swap crisis, but stocks devalued due to restrictions imposed by governments, rather than due to financial scams.

One of the first econometric tools that registered market ferment was the (VIX)[7]. Data show how U.S. market volatility began rising in January, climbed in February, and peaked in March[8]. Despite offering a clear-cut representation, a more thoroughly analysis is necessary to fully grasp the main causes for this unprecedented shock. Differently from past pandemics, the mortality rate was not as high (the Spanish Flu, by contrast, is estimated to have reduced world population by 2 %[9]); however, in this case, news on the pandemic monopolised daily newspapers, and resulted in sudden shocks when organized exchanges opened the following days[10]. Another key element which contributed to the rapid downfall of market prices is government restrictions. In fact, despite having substantially reduced the potential toll of the pandemic, government decisions drastically impacted on businesses[11] – mostly the energy,

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[6] *See* Binxin Yan et al., *Analysis of the Effect of COVID-19 On the Stock Market and Potential Investing Strategies* (2020), SSRN, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3563380 The paper shows how the 2003 virus's effects lasted no more than a couple months as it took 3 months for the Dow Jones to rise back to its peak.

[7] A calculation designed to produce a measure of constant, 30-day expected volatility of the U.S. stock market, derived from real-time, mid-quote prices of S&P 500® Index (SPX℠) call and put options.

[8] *See* Baker, *supra* note 5 where he stated: "COVID-19 volatility surge began in the fourth week of January, intensified from the fourth week of February, and began tapering in the fourth week of March". Baker analysed daily market reactions (jumps bigger than 2.5 %) to published news and reported: "Spanish Flu triggered not a single daily stock market move of 2.5 percent or more, while developments related to COVID-19 triggered two dozen such jumps".

[9] *Id.* at * 3.

[10] *Ibidem.* Baker further noted: "By March, COVID-19 developments receive attention in more than 90 % of all newspaper discussions of market volatility and policy uncertainty". *See also* Raffaella Meninno & Guntram Wolff, *As the Coronavirus spreads, can the EU afford to close its borders?* (2020), VOXEU, https://voxeu.org/content/coronavirus-spreads-can-eu-afford-close-its-borders.

[11] *See* Richard Baldwin, *The Supply Side Matters: Guns versus Butter, COVID-Style* (2020), VOXEU, https://voxeu.org/article/supply-side-matters-guns-versus-butter-covid-style as he stated: "COVID-19 and the containment policies have directly and massively reduced the flow of labour to businesses. The result has been a sudden and massive reduction in the output of goods and services".

travel and entertainment industries – by imposing social distancing and closing frontiers, thereby prohibiting travelling across countries[12]. This striking evidence shows how an interconnected world is comparable to leverage in financial budgeting decisions: it increases upside potentials (by lowering transport costs, tariffs and increasing trade) but, at the same time, amplifies sudden shocks.

Nevertheless, capital markets recovered from the downfall in a quite short period of time. One year after, U.S. stock prices had almost returned to their pre-pandemic levels and the generated crisis seemed not to have occurred[13]. Economies benefited from the fast recovery, and Countries employed both fiscal and monetary policies to restore the equilibrium and avoid further shocks. However, companies had to adapt to the new conditions and, throughout 2020, they were vulnerable to corporate raiders attempting to hoard shares at discount. The predicted scenario represented a threat for companies, as share prices did not represent their intrinsic value. Boards therefore responded by setting up defensive mechanisms to fend off hostile takeovers and serve the shareholder value.

At the strike of the pandemic, a well-known device, deeply used toward against hostile bids in the last two decades of the previous Century, returned to vogue: the shareholder rights plan. This unconventional and aggressive instrument saw the light of the day in 1982, during the 1980s takeover wave[14], when Martin Lipton[15], considered the father of the pill, introduced it in the corporate governance environment defending El Paso Electric against American General Oil. It gained momentum and was used in 1983 during the takeover contest between Brown Foreman and Lenox, as a response to tender-based hostile takeovers, and, despite its ups and downs, has been adopted whenever a crisis occurred, or when defending against very powerful bidders[16].

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[12] *See* the chart by the Transportation security administration (TSA) which points out that daily flights reduced by 94 % in the U.S., https://www.tsa.gov/coronavirus/passenger-throughput.

[13] *See* Patti Domm, *A stunning fall and a recovery: How the stock market has evolved one year since Covid hit* (2021), CNBC, https://www.cnbc.com/2021/03/12/a-stunning-fall-and-a-recovery-how-the-stock-market-has-evolved-one-year-since-covid-hit.html She reported: "*A year after the Covid pandemic shut down the economy, stocks have gained 79 % from the lows*". *See also* Karl Russell & Mohammed Hadi, *The stock market's covid pattern: faster recovery from each panic* (2021), New York Times, https://www.nytimes.com/interactive/2021/12/07/business/omicron-stock-market-covid.html.

[14] For a broader perspective, *see* Andrei Shleifer & Robert W. Vishny, *The Takeover Wave of the 1980s*, 249 Science 745-749 (1990).

[15] Martin Lipton is is an American lawyer, a founding partner of the law firm of Wachtell, Lipton, Rosen & Katz specializing in advising on mergers and acquisitions and matters affecting corporate policy and strategy.

[16] Just recently they have been used by Twitter board to defend against Elon Musk. *See* Lauren Feiner, *Twitter board adopts 'poison pill' after Musk's $43 billion bid to buy company* (2022), CNBC, https://www.cnbc.com/2022/04/15/twitter-board-adopts-poison-pill-after-musks-43-billion-offer-to-buy-company.html.

Delaware's jurisprudence, the well-recognized authority in corporate law[17], has ruled over many cases of poison pills adoption and consolidated its position over this type of defensive tactic by imposing the burden of proof to show the reasonability of the threat and the proportionality of the response on directors. However, this stringent standard and usual adversity of proxy advisors have led directors to shift away from this defensive tactic whenever facing a takeover threat.

Nevertheless, in time of market turmoil, directors often turn to this measure to fend off potential hostile bids. It is what occurred in the first quarter of 2020 when, as a result of market disruption, company's boards massively employed this kind of measure[18]. In fact, during March there were 22 active poison pills (17 traditional and 5 NOL[19]). In relative terms, only in that month, the overall number of pills increased fivefold compared to the previous 3-year period[20]. As predicted before, however, as the most dramatic months of the pandemic passed by and the economic recovery gained momentum, most companies redeemed their poison pills[21].

The presented evidence is in line with what the theory predicts as, due to the spread of the contagion and subsequent government restrictions, companies sought their balance sheets worsening, and their stock price dropped; in turn, they found themselves exposed to hostile takeovers as market prices did not respect their fundamental value. Moreover, bidders tried to benefit from the situation by hoarding company's stocks at discount. In addition, this peril loomed over the corporate environment as shareholders and companies themselves were in

[17] *See* Pierluigi Matera, *Delaware's Dominance, Wyoming's Dare. New Challenge, Same Outcome?*, 27 (1) Fordham J. on Corp. and Fin. Law 73-139 (2022).

[18] *See* Ofer Eldar & Michael Wittry, *The Return of Poison Pills: A First Look at "Crisis Pills"* (2020), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2020/05/06/the-return-of-poison-pills-a-first-look-at-crisis-pills/ where they reported: "Until the emergence of COVID-19, the number of active poison pills in US corporations was extremely low. Although historically popular, particularly in the merger waves of the late 1980s and 1990s, poison pills have fallen out of favor in the last two decades, in large part due to the influence of proxy advisors; at the end of 2019, only 25 S&P 500 public firms had an active positive pill". In only two months, instead, in March and April, "at least 45 firms have announced the adoption of poison pills".

[19] *See* Keith Gottfried & Sean Donahue, *The Misplaced Focus of the ISS Policy on NOL Poison Pills* (2018), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2018/08/16/the-misplaced-focus-of-the-iss-policy-on-nol-poison-pills/ . As they put it, "an NOL poison pill is intended to deter any person from acquiring beneficial ownership of 4.99 % or more of the company's common stock without the approval of the company's board of directors" and, differently from a conventional pill it is used by companies when underperforming due to structural reasons (and therefore reporting a Net operating loss in their financial statement) rather than to contrast a shark's bid.

[20] *See* Sanjay M. Shirodkar et al., *The Rise of the Aggressive Poison Pill* (2020), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2020/04/24/the-rise-of-the-aggressive-poison-pill/.

[21] *See* John Jenkins, *Poison Pills: 2020-2021 Pill Adoptions* (2021), DealLawyers.com, https://www.deallawyers.com/ blog/2021/08/poison-pills-2020-2021-pill-adoptions.html for an in-depth analysis.

desperate need of cash – the so-called liquidity crisis[22] – and were willing to accept a lower remuneration for their shares. As a consequence, defensive tactics – and especially poison pills – seemed the optimal choice to contrast a non-negotiated offer, as it is common for companies to deploy shareholder rights plans when prices are deflated.[23] For what concerns the consequent increase in companies' prices, however, it is not fully clear whether the adoption of a shareholder rights plan adequately effects market value, and thus stabilises prices, or the appreciation is only a simple mean-reversing effect[24], given the sharp drop experienced.

So far, poison pills seemed to be tailor made to guard against a hostile bid, however directors are vested with a rather difficult task, which is balancing the diverse – and sometimes contrasting interests – of corporate constituencies. It is possible to list 3 key conflicts, as a bare minimum, emerging in a takeover context: firstly, the one between directors and shareholders, secondly the one between different classes of shareholders, and finally the one between the company and the raider.

For what concerns the first conflict of interest it arises out of the delegation principle companies pose on. The implied risk for the company is, on one side, to have directors entrenching themselves and, on the other, to not being able to maximise shareholder value due to the suppressed price, should directors avoid employing defensive mechanisms. The second is referred to the different power shareholders enjoy, as majority ones may influence corporate decisions and exploits benefits at the expenses of the minority[25]. Moreover, while choosing the optimal defence to guard against a corporate raider, the long-standing debate concerning the purpose of a corporation arises: should a corporation achieve the best achievable result for present company's shareholders, or try to maximise the long-term value, regardless of current shareholders' interests?[26]. Finally, directors are aware that, when there is a change in control,

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[22] *See* Mike Harmon & Victoria Ivashina, *Managing the Liquidity Crisis* (2020), Harv. Business Rev., https://hbr.org/2020/04/managing-the-liquidity-crisis where they call for a government intervention to avoid bankruptcy of already highly leveraged firms, an easier access to private equity for small firms and a lax policy of the Fed on collateralized requirements.

[23] *See* Emiliano M. Catan, *The Insignificance of Clear-Day Poison Pills*, 1 J. Leg. St 12 (2019).

[24] *See* Lina Saigol & Selin Bucak, *Companies race to swallow poison pills to thwart hostile bids as stock prices plunge* (2020), Marketwatch.com, https://www.marketwatch.com/story/companies-race-to-swallow-poison-pills-to-thwart-hostile-bids-as-stock-prices-plunge-. As the article shows: *"*stock prices of companies in these highly exposed sectors experienced a dramatic rise following the adoption of poison pills*"*.

[25] *See* Janis Berzins et al*.*, *Shareholder Conflicts and Dividends* (2017), ECGI, https://ecgi.global/working-paper/shareholder-conflicts-and-dividends where they show how, in the "opportunistic model", "as a result, majority shareholders may use their control rights to capture private benefits".

[26] *See* William T. Allen et al., *The Great Takeover Debate: A Meditation on Bridging the Conceptual Divide,* 69 U. Chi. L. Rev.1067-1101, 1071 (2002). The paper counterposes the two models – property and entity – which advocate respectively for a maximisation of current shareholders and of the long-term value of a corporation.

the new owners replace management[27]; therefore, it is not unusual for the formers to attempt to stay in charge by deploying very aggressive defensive tactics, which may in turn disserve the shareholder value by effectively reducing external funding.

Delaware's jurisprudence has intensively ruled over the matter and has attempted to curb those conflicts of interest by imposing penalties on directors. Consequently, they should be very careful in adopting a specific defensive tactic, as their choice can result in conviction. Despite the standard used by courts to scrutinise managers' decisions is firm by now, during the early stages of pandemic, certain companies, operating in the worst-hit industries, employed unconventional pills as the question whether courts would have allowed a so-called "crisis pill" was open. Delaware, with a Chancery Court decision[28] which was later affirmed in the Supreme Court[29], made clear that aggressive pills will be invalidated under Delaware law; but in its ruling, it may have left the door ajar. To fully analyse the matter and make predictions on future applicability of the pill, it is necessary to present in detail the context of a takeover.

B. Boards' nuclear weapon: the shareholder rights plan (poison pills)

1. Context of a poison pill

Takeovers represent a turning point in the company's life as bidders usually try to gain control when companies are in distress to apport changes in the management structure and put the company back on track. At the same time, takeovers may be deemed useful to reduce the agency cost between directors and shareholders because they perform an efficiency task through which the market for corporate control replaces underperforming managers[30]. In particular, in public companies, takeovers gained momentum because the structure of dispersed ownership renders shareholders' monitoring activity over directors even harder.

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[27] The concept of change in management when a takeover occurs is expressed in this article. *See* Tobias Umbeck & Adrien Bron, *Change Management in Merger Integration* (2017), Bain & Company, https://www.bain.com/insights/change-management-in-merger-integration/.

[28] *See Williams supra* note 2.

[29] *See Williams supra* note 3.

[30] For a more in-depth analysis on the origins of the market for corporate control *see* John Armour & Brian Cheffins, *The Origins of the Market for Corporate Control*, 5 U. Ill. L. Rev. 1835-1866, 1835 (2014) where they pose that the market for corporate control "took on its modern form in the mid1950s with the emergence of the cash tender offer" and that "the way in which cash tender offers came to dominate the market for control after World War II can be explained primarily by changes in the pattern of share ownership and reduced opportunities bidders had for "managing" the stock price of intended targets".

When companies are mismanaged, share prices drop, the corporations are therefore weaker and exposed to takeover attempts from bidders which commonly see themselves as the ones in charge of shifting the downward momentum. Moreover, takeovers represent a compensation for shareholders because they obtain a premium[31] as a restoration for past mismanagement and as a reward for control acquired through those stocks. Despite the monitoring role conferred by corporate law to takeovers, there is still great uncertainty and disagreement whether they increase or not firm's value. On one side, it can be argued that they sensibly affect corporate performances[32] when managers are replaced as a consequence of the change in control; whilst it is also true that, if overpriced, they can ruin firm's value[33].

Takeovers are also very problematic because two contrasting interests occur: directors are willing to impede bidders from acquiring control (and therefore remain in charge) whilst shareholders usually aim to realise a quick profit. In addition, the formers, which are appointed to manage the company for the interests of stockholders and normally owe their fiduciary duty to the corporation, owe those duties to each shareholder, in a takeover context. This is a distinguishing element, as there are certain implications from it[34]. Moreover, it is not an easy task for directors to balance the interests of the different shareholders, given that the formers owe those duties to the whole class of shareholders. In fact, research shows that it is difficult

[31] On average the premium amounts to 25-30 % of company's price. *See* Jens Kengelbach et al., *The 2019 M&A Report: Downturns Are a Better Time for Deal Hunting* (2019), Boston Consulting Group, https://www.bcg.com/it-it/publications/2019/mergers-and-acquisitions-report-shows-downturns-are-a-better-time-for-deal-hunting.

[32] In favour of this thesis, *see* Michael C. Jensen & Richard S. Ruback, *The market for corporate control: The scientific evidence*, 11 J. Fin. Econ. 5-50, 5 (1983) where they argue: "evidence indicates that corporate takeovers generate positive gains, that target firm shareholders benefit, and that bidding firm shareholders do not lose. The gains created by corporate takeovers do not appear to come from the creation of market power. With the exception of actions that exclude potential bidders, it is difficult to find managerial actions related to corporate control that harm shareholders".

[33] More recent studies, instead, predict gains from takeovers only for some specific companies (*i.e.,* small firms) or even posit most takeovers fail. S*ee* Sara B. Moeller et al., *Do Shareholders of acquiring firms gain from acquisitions?* (2003), NBER working paper no. 9523, https://www.nber.org/papers/w9523 where they posit: "Mergers and acquisitions destroy shareholder wealth in the acquiring companies. Research shows that, over the past 20 years, U.S. takeovers have led to losses of more than $200 billion for shareholders". They further note that small firms usually gain while big firms lose from a takeover. *See also How mergers go wrong* (2020), The Economist.com,https://www.economist.com/leaders/2000/07/20/how-mergers-go-wrong. And, for the detailed reasons why a merger goes wrong *see* Nuno Fernandes, *The Value Killers* (2020), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2020/01/08/the-value-killers/ .

[34] *See* Dean G. Smith, *The Critical Resource Theory of Fiduciary Duty*, 55 Vand. L. Rev. 1399-1497, 1401-1402 (2002) for a deeper understanding. He also explains what the duties were introduced for, as he posits: "every relationship properly designated as fiduciary conforms to the following pattern: one party (the fiduciary) acts on behalf of another party (the beneficiary) while exercising discretion with respect to a critical resource belonging to the beneficiary".

to see how diverging interests of different classes of shareholders can be made to coalesce whilst maintaining the best interests of the company as the common vision[35].

Another risk takeovers may entail is that directors would pursue a short-term strategy, given that they are commonly replaced whenever a change of control occurs. As an example, directors may pursue strategies to pump share prices, rather than focusing on the fundamental long-term interest of the company. As an example, in the Twitter takeover happened at the end of April 2022 the price paid was $54.20[36] per share (and that includes a 38 % premium on the pre-announcement stock price), while the company traded roughly at about $ 70[37] just one year ago. One could then argue that directors focused on short-termism rather than long-termism.

The chances of success for a takeover are higher the shorter it lasts; therefore bidders, and by consequence directors, act in a time-sensitive setting. The federal legislator consequently intervened to extensively rule the most common type of takeover: the tender offer. Bidders are subject to the § 13 (d)[38] of the *Williams Act*, which specifically impose disclosure when acquiring shares. It is in the bidder's interest to maintain the confidentiality and secrecy of the transaction because, should anyone know of the deal, competitive bidders may step in and share prices would therefore skyrocket as an auction can quickly take place. Further, directors could deploy defensive tactics mainly for one reason: the substantial risk of being removed when the new owner acquires control. On the other side, the target board needs to abide by § 14 (d), which imposes precise procedural rules and disclosure requirements. To

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[35] *See* Beatriz Pessoa de Araujo & Adam Robbins, *The Modern Dilemma: Balancing Short- and Long-Term Business Pressures* (2019), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2019/06/20/the-modern-dilemma-balancing-short-and-long-term-business-pressures/ . They continue the analysis by stating: "This can leave boards with the dilemma of how to fulfil their duties to the company (and do so for the benefit of all shareholders) while taking into account the impact of board decisions on all company stakeholders. The shareholder base's diverse expectations are an added complication when attempting effectively to balance the need for short-term results with the company's longer-term aspirations". They finally conclude: "shareholders do not own the business enterprise itself; shareholders own shares in companies and their rights are the rights attached to those shares". Therefore, the final choice of how to deal with this opposing interest shall be addressed by the directors by virtue of the principle of the separation of ownership and control.

[36] *See* Michelle F Davis & Liana Baker, *Twitter Takeover Was Brash and Fast, With Musk Calling the Shots* (2022), Bloomberg.com, https://www.bloomberg.com/news/articles/2022-04-26/twitter-takeover-was-brash-and-fast-with-musk-calling-the-shots .

[37] *See* Lauren Hirsch et al., *Twitter Nears a Deal to Sell Itself to Elon Musk* (2022), N.Y.times.com, https://www.nytimes.com/2022/04/24/technology/twitter-board-elon-musk.html where they report: "Several analysts have said they expected Twitter's board to only accept a bid that valued it at a minimum of $60 a share. Twitter's stock rose above $70 a share last year".

[38] More specifically, regulators stated that: "any person who acquires beneficial ownership of more than 5 % of the outstanding shares of any class of voting equity securities registered under Security and Exchange Act § 12 must file a Schedule 13 D disclosure statement within 10 days of such acquisition with the SEC, the issuer, and the exchanges on which the stock is traded"; s*ee generally* Stephen M. Bainbridge, *Mergers and Acquisitions*, *in* CORPORATE LAW 431–448 (4th ed. 2020). The 5 % level represents the trigger threshold; therefore bidders usually try to hoard an amount of shares slightly below that level before disclosing it to the board. This section was introduced in the Security and Exchange act of 1934 to regulate the so-called beachhead acquisitions which occur before the bidder has the duty to disclose.

determine whether the transaction at stake should be deemed a tender offer, and thereby subject to § 14 (d) and the underlying rules, courts will look at the eight-factor test: the *Wellman* test[39].

Following to this overview of the puzzling events in a takeover scenario, it seems crystal clear that the jurisprudence faced a rather difficult task in finding the right standard to rule over the subject; namely to introduce a rule suited to delineate the admissible and forbidden directors' conducts. As a direct consequence of a takeover, directors could in fact deploy defensive tactics, but must be careful to maximise the shareholder value while still allowing a desirable acquisition to go forward. Thus, directors face a quite difficult task in deciding how to intervene to fulfil their fiduciary duties towards the shareholders, and deploying the right defensive tactic is rather complicated; especially considering the implications it may have (market impact, possible court litigation, etc.). Despite it should be clear by that boards employ defensive mechanisms to respond to a takeover, it is worthwhile to consider the supporting views for the deployment of the said tactics.

There are four easily identifiable reasons behind the employment of a defensive mechanism which are: to avoid inefficient acquisitions, allow the board to negotiate a higher price – thereby maximising the shareholder value –, facilitate investment efficiency, and carefully balance the benefits and downsides of the acquisition so to take measures in the interests of stakeholders.

The first rationale rejects the assumption that the market for corporate control prices companies accurately. In fact, supporters of this view believe that, if a company is under-priced and a potential acquirer presents an offer which doesn't fully reflect the company's value, directors should be allowed to oppose it. This theory poses on the belief that the board possesses

[39] It was first used in the decision *Wellman v. Dickinson*, 475 F. supp. 783, 823 (S.D.N.Y) and contains a list of factors to be met for a transaction to be deemed a tender offer; however, it is unclear how many of them must be fulfilled. Therefore, it causes ambiguity as the choice will be performed by the Court case-by-case. Specifically, the factors are: (i) whether there is an active and widespread solicitation of public security holders (ii) whether the solicitation is made for a substantial percentage of the issuer's securities (iii) whether the offer is made at a premium over the prevailing market price (iv) whether the terms of the offer are firm rather than negotiable (v) whether the offer is contingent upon the tender of a fixed minimum, and perhaps subject to the ceiling of a fixed maximum number of securities to be purchased (vi) whether the offer is open for only a limited period of time (vii) whether the offerees are subjected to pressure to sell (viii) whether the public announcements of a purchasing program precede or accompany a rapid accumulation of large amounts of the target company's securities.

private information and shall know what the intrinsic value of the firm is[40]. Consequently, it should reject an offer which is below the fundamental value of a firm because "coercive".[41]

The second emphasises the board's negotiation function, as it possesses a stronger bargaining power compared to the shareholders and would therefore obtain a higher closing price for the deal[42]. This theory hinges on the dispersed ownership structure[43] public companies have and concludes that stockholders would accept any offer that is nontrivially above the share price. In fact, if on one side dispersed ownership has allowed even small investors to access the market, it is also true that diverging interests amongst shareholder classes can lead to disunity, which in turn could negatively affect the price agreed for an acquisition. This rationale is in line with what the DGCL prescribes[44]: "The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors*"*. And given that directors have the power to manage the corporation, it is their duty to negotiate what is best for the firm.

Two main implications of this distributional rationale are to be noted: board's defence may result in inefficient income – given the increased capital required to perfect the transaction, resulting in a social deadweight loss – and the economic problem stemming from the adoption. In particular, the ability to deploy a defensive tactic, gives a board the power to increase the price the target can command conditional on receiving a bid. As previously stated, this might apport a benefit to the firm as the initial bidding price may not respect the intrinsic value; however, it may also increase the probability of not receiving further offers because bidders'

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[40] *See* Ronald J. Gilson & Alan Schwartz, *An Efficiency Analysis of Defensive Tactics*, 11 Harv. Bus. L. Rev. 1-54, 4-5 (2021). They show this by providing an example that, when a company is priced at $ 7 per share and the board reasonably believes the fair price should be $ 10, directors should have the power to reject a $9.5 offer, despite a sensible 35 % premium.

[41] According to Delaware courts, a takeover bid "substantively coerces" target shareholders when it offers them the opportunity to accept a bid that may be below the "true" value of the company, but the shareholders will not recognize that their company is under-priced. In the said case, they would not have recognized that the $ 9.5 offer was coercive, while they would notice the 35 % premium on the suppressed price. *See* Edward G. Fox et al., *Economic Crisis and the Integration of Law and Finance: The Impact of Volatility Spikes*, 116 Colum. L. Rev. 325-407, 398–406 (2016). *See also* Ronald J. Gilson & Reinier Kraakman, *Delaware's Intermediate Standard for Defensive Tactics: Is There Substance to Proportionality Review?*, 44 Bus. Law. 247-274, 260 (1988).

[42] *See* Martin Lipton, *Takeovers in the Target's Boardroom*, 35 Bus. Law. 101-134, 106–109 (1979) for the target board discretion argument.

[43] For an analysis of the causes of dispersed ownership in the corporate world, *see* John C. Coffee Jr, *Dispersed Ownership: The Theories, the Evidence, and the Enduring Tension Between 'Lumpers' and 'Splitters'*, Columbia Law and Economics working paper no. 363 (2020), https://ssrn.com/abstract=1532922 . He sustained: "dispersed ownership arises principally from private ordering. Intermediaries fill the void created by legal shortcomings and create bonding mechanisms that allow dispersed ownership to spread beyond the limited geographic area in which the founding entrepreneur is known and trusted". He went on by stating: "the appearance of numerous minority shareholders, gradually spreading across a broad geographic area and the break-up of controlling blocks" occurred mostly in the 1980s, were the two steps leading to a dispersed ownership structure.

[44] Del. Gen. Corp. Law § 141 (a).

profits from the acquisition will diminish. Thus, a board acts in the interests of its shareholders only if it deploys the right combination of defensive tactics that optimally trades off bid size and bid frequency. Moreover, rejecting an offer to remain independent, or equivalently deploying an exceptionally aggressive defensive tactic, may result in board's entrenchment, thereby causing a detriment to the shareholders.

The third rationale – the so-called investment efficiency – for the adoption of a defensive tactic is rather complicated because it concerns the risk that the market might overvalue a short-term investment while under-pricing a longer-term one. Whenever a board must choose amongst projects with a different time horizon, it shall consider what is best for the company. And, if it is not fairly priced by the market, it shall have the authority to employ a defensive tactic to resist bidders, until the project realizes. Potential acquirers, in fact, may be attracted by the discrepancy between firm's value and trading price and may attempt to obtain control enjoying the benefits of the investment at discount.

Finally, the fourth, probably the most debatable rationale, is that companies are a founding element of capitalism, and allowing directors to employ defensive mechanisms when they deem necessary to do so may serve the interests of the whole stakeholders (*i.e.,* suppliers, employees, etc.). The board in fact possesses the material information to carefully evaluate the transaction and can weigh the benefits or the shareholders and the costs for the stakeholders.

Having listed the main reasons in favour of employing a defensive tactic, and before delving into the technicalities of the shareholder rights plan, mentioning another common mechanism – often used in conjunction with poison pills – serves the purpose of providing a typical anti-takeover combination boards adopt. The said defence is the staggered board.

It is a peculiar provision that divides directors in more than one class – typically three – of which only one is elected annually. This measure is particularly effective as it delays the acquisition process and is even more suited to deter any takeover attempt when in conjunction with a poison pill. In fact, the bidder faces both a dilution of its own shares and a sensible prolongation of the time to effectively complete the acquisition. Namely, staggered boards, or equivalently classified boards, provide anti-takeover protection both by forcing any hostile bidder, no matter when it emerges, to wait at least one year to gain control of the board and requiring such a bidder to win two elections far apart in time rather than a one-time referendum on its offer[45].

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[45] *See* Lucian A. Bebchuk et al., *The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence and Policy*, 54 Stan. L. Rev. 887-951 (2002) for an extensive study of the effect classified boards produce in the market for corporate control.

This defensive tactic has gained momentum with the appearance and proliferation of poison pills. Takeover law, in fact, allows managers to maintain a pill and thereby impede a hostile bid, as long as they are in office. As a result, when managers maintain their opposition to a hostile bid, the bidder can obtain control only if it replaces the incumbent board and appoints new directors to redeem the pill. The acquirer must operate via a ballot box victory to win control of the board – which is the safety valve on which takeover law has relied to protect shareholders as it sensibly complicates the process.[46] While the tactic proved very effective to thwart hostile bidders, it can be improperly used to insulate target directors at the shareholders' expense[47]. It has been demonstrated in fact, that the defence does not apport a material benefit to the shareholders (in terms of premiums on the price agreed)[48] but rather limits itself to hindering an acquisition process.

Regardless of the outcome of an acquisition, during the 1980s and 1990s takeover waves[49] the debate over the effective benefits or downsides of acquisitions gained momentum.

Namely, the following questions arose: should management of the target company be allowed to resist a hostile tender offer in order to remain independent? And which, if any, of the various "shark repellent" measures by which a potential target can make itself unattractive to a bidder are justified? Moreover, do hostile takeovers in the aggregate promote economic efficiency or only a preoccupation with short-run profit maximization at the expense of strategic planning, research, and innovation?[50]. Theorists and people familiar with the matter started to take sides. The takeover inclined view had Professor Lucian A. Bebchuk[51] as one of its most fervent supporters and the opposite side was sustained by the attorney Martin Lipton[52].

The debate went on for many years, and still today the question is unsolved. However, as the number of takeovers was rapidly increasing, boards began to adopt unconventional defensive tactics, as many lawyers innovated the sector by introducing both pre-bid and post-bid defensive mechanism. A typical example of a pre-bid defence is the said staggered board,

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[46] *Id.* at 907.
[47] *Id.* at 891.
[48] *Ibidem.*
[49] *See* Shleifer & Vishny *supra* note 14.
[50] *See* John C. Coffee, *Regulating the market for corporate control: a critical assessment of the tender offer's role in corporate governance,* 84 Colum. L. Rev. 1145-1296 (1984) for a broader analysis.
[51] Amongst the masterpieces written by him, *see* Lucian A. Bebchuk, *The Case for Facilitating Competing Tender Offers*, 95 Harv. L. Rev. 1028-1056 (1982).
[52] For the opposing view, *see* Martin Lipton, *Takeover Bids in the Target's Board- room: A Response to Professors Easterbrook and Fischel*, 55 N.Y.U. L. Rev. 1231-1236 (1980).

while a post-bid example can be a stock lockup, which is a mechanism that grants the favoured bidder a competitive advantage over the others[53].

As anticipated, many of these measures were developed in the last two decades of the 20th Century; specifically 1982 signalled a new era for vigorous takeover defences had just started, as Martin Lipton introduced a brand-new defensive mechanism: the shareholder rights plan, or commonly known as poison pill. When the former Texas tycoon and chairman of Mesa petroleum[54],T. Boone Pickens, aimed to take over the Texan-based General American Oil Company, the lawyer proposed the first prototype of poison pill. The board opted not to use the defensive tactic[55]; but this was only the preamble for an intensive use of the aforementioned defensive mechanism. In fact, few months later, El Paso electric's board employed a shareholder right plan to defend against General American Oil.

The usage of poison pills then skyrocketed as they proved to be very effective to thwart a hostile takeover. Nevertheless, as the golden age of takeovers came to an end, and due to a very strict standard consolidated[56], the fashion of this unconventional defensive tactic ended.[57] This evidence suggests that, whenever in danger, boards look back at poison pills as they are aware of the substantive dilution potential acquirers will incur in, should they proceed with a coercive acquisition mechanism.

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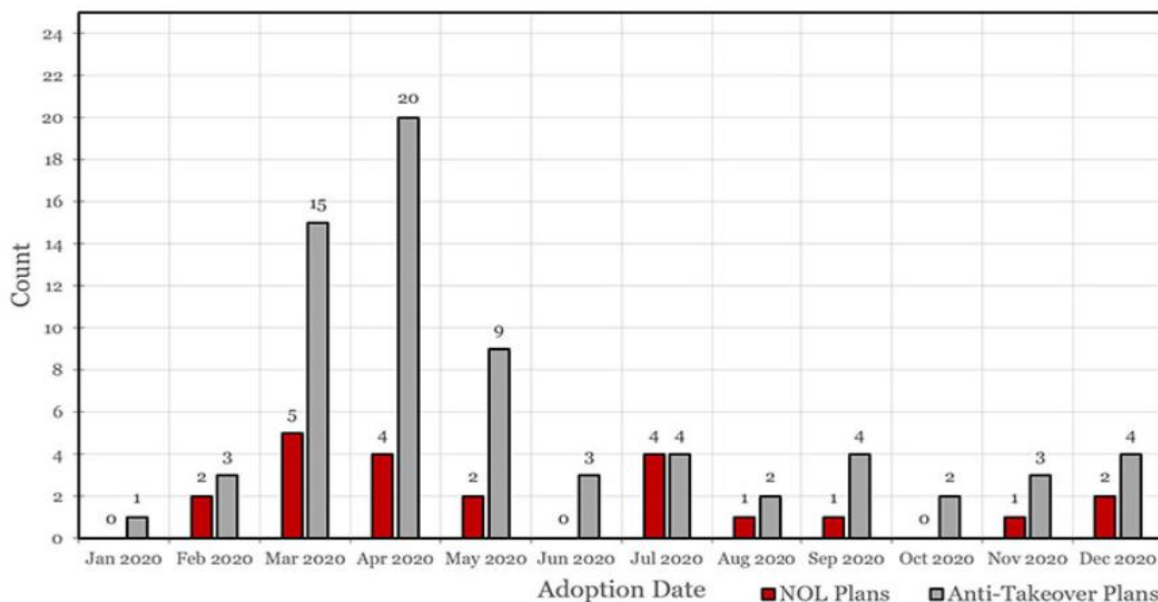
[53] Stock lockups options give the favoured bidder an option to purchase treasury or authorized but unissued target shares. If the option is exercised prior to the shareholder vote on the merger agreement, the favoured bidder can vote the additional shares in favour of the merger, helping to assure that the requisite approval will be obtained. If a competing bidder prevails, the holder of the option could still exercise the right and obtain valuable stocks at discount and therefore sell them on the market realising a quick profit. *See* Stephen M. Bainbridge, *Corporate Law*, § 12. 8 (4th ed. 2020).

[54] *See* John Greenwald, *High Times for T. Boone Pickens* (1985), Time, https://content.time.com/time/subscriber/article/0,33009,961946,00.html.

[55] The board was worried that employing the defensive tactic would have resulted in conviction for themselves, as the tactic's legality had not been tested, and preferred not to use it. *See* Norma Cohen, *US companies fend off activists with poison pills* (2014), Financial Times, https://www.ft.com/content/b78ffe52-cada-11e3-9c6a-00144feabdc0.

[56] Courts use the *Unocal* test when evaluating a poison pill, which shifts the burden of proof that a reasonable threat was present, and a proportional response was taken to fend off the hostile bid. The standard comes from the decision in *Unocal Corp. v. Mesa Petroleum Co.* - 493 A.2d 946 (Del. 1985) and will be extensively treated in the part III.

[57] This is expressly reported in Beth E. Berg et al., *ISS Signals: More Understanding for Poison Pills and Skepticism for Activist Campaigns During the COVID-19 Crisis* (2020), https://corpgov.law.harvard.edu/2020/04/11/iss-signals-more-understanding-for-poison-pills-and-skepticism-for-activist-campaigns-during-the-covid-19-crisis/.They note how, at the end of 2019, before the COVID-19 related news reverberated on financial markets, only 25 out of the S&P 1500 had a poison pill in place. However, they added that, in just a month from March to April, 28 U.S. public companies adopted the defensive tactic. They continued that was the highest number of new adoptions of poison pills in such a short period.



The graph above[58], offers a thorough explanation of what has just been stated, focusing on the recent pandemic. The number of poison pills adopted by U.S. companies sharply rose at the outbreak of the pandemic following to the three daily record drops, respectively in 9, 12 and 16 March[59]. It even climbed in April, as many boards employed the defensive mechanism to fend off corporate raiders but, as the worst moments of the crisis came to an end, the number gradually returned to its pre-COVID-19 average.

Now that the context directors operate in, the defence mix they can deploy, and the sustaining arguments for the employment of those tactics when facing a hostile takeover have been presented, the discussion flows to the specific type of anti-takeover mechanism: the poison pill.

2. The features of a shareholder rights plan

[58] *See* Mara Elyse Goodman et al. (2021), *2020 Poison Pill Recap and Current Trends*, JDSupra.com, https://www.jdsupra.com/legalnews/2020-poison-pill-recap-and-current-9229924/.

[59] *See* Liz Frazier, *The Coronavirus Crash Of 2020, And The Investing Lesson It Taught Us* (2020), Forbes.com, https://www.forbes.com/sites/lizfrazierpeck/2021/02/11/the-coronavirus-crash-of-2020-and-the-investing-lesson-it-taught-us/?sh=c492af046cfc where she documented the crash caused an escalation of 7.79 %, 9.99 % and 12.9 % drop in the Dow Jones Industrial average index. The fall was so damaging for the U.S. economy, and unjustified to a certain extent, that the New York Stock Exchange closed for several hours.

Poison pills are defensive tactic than can be adopted by a board without shareholder approval[60], "on a clear day" and that normally last no more than a year[61]. They may differ from one another, but they all share certain two fundamental characteristics: a triggering threshold and a definition of beneficial ownership. The basic shareholder rights plan, provides that, whenever a corporate raider acquires share ownership above the triggering threshold, target company stockholders are given the opportunity to buy target's shares at discount. The bidder will therefore suffer share dilution and will find it difficult to obtain control without reaching an agreement with the target's board. This ingenious mechanism therefore hinders raider's takeover attempt because share acquisition will cause the shareholder right plan to release its effects[62] and will allow all the former stockholders (except for the raider itself) to benefit from the plan.

The definition of beneficial ownership is provided in the *Williams Act* of 1968 – which amended the *Security and Exchange Act* of 1934[63]. A shareholder is deemed to have acquired beneficial ownership whenever it purchases 5 % of the outstanding shares of any class of voting equity securities registered under Sec. Ex. Act § 12. Consequently, the act requires disclosure by filing a Schedule 13D[64] within 10 days of such acquisition. Turning to the triggering threshold, instead, a typical plan consists of a 15 - 20 percent trigger threshold. However, it is common practice to include a two-tiered trigger level depending on the type of acquisition and to exempt special stockholders as the institutional investors[65]. As an example, directors are used to set a triggering percentage of 15 - 20 percent in a hostile takeover as the acquiror's

[60] *See Account v. Hilton Hotels Corp*., 780 A.2d 245 (Del. 2001) where the Supreme Court affirmed the decision of the lower court reporting: "directors of a Delaware corporation may adopt a rights plan unilaterally".

[61] *See* Goodman *supra* note 58. The article provides that "most rights plans provide that the rights expire 364 days after the adoption of the rights plan", and the duration is in line with ISS and Glass Lewis' s guidance. Companies usually abide by the guidelines as these two proxy advisors are powerful and, if a board's decision is contrary to the guidance provided, they will almost certainly recommend shareholders to express a no vote for directors in the following annual meeting.

[62] To see why they got their nickname "poison pills" *see* Farah Mohammed, *Why Companies Swallow Poison Pills* (2019), Jstor.com, https://daily.jstor.org/why-companies-swallow-poison-pills/.

[63] 15 U.S.C. § 78a et seq.

[64] The crucial items for this schedule are item no. 2 on bidder's identity, item no. 4 on disclosure of intent, and no. 6 on disclosure of agreements and understandings. In the first, filers must report any conviction during the preceding 5 years, except traffic violation or misdemeanours, and if they were the subject of a judgment on the violation of securities laws – if the purchaser is a natural person – or any conviction of executive officers and directors and controlling shareholders – if the offer comes from an artificial person. The second prescribes filers to report any plans or proposals which the reporting persons may have, which relate to or would result in any of certain specific actions. It is the most problematic item and, by consequence, the most litigated at court. Finally, item no. 6 mandates to report any contract, arrangements, understandings, or relationships with respect to the securities of the issuer.

[65] *See* Goodman *supra* note 58, "some rights plans in fact bifurcate the trigger, setting a higher triggering percentage for passive investors (*e.g.*, Schedule 13G filers) and a lower, general triggering percentage. If the general triggering percentage is set below 15 %, most recent plans bifurcate the trigger, with the higher triggering percentage typically being set at 20 %".

objective would typically be to buy 100 % of the company or, at least, a controlling interest. In this case, a higher triggering percentage will still serve the rights plan's purpose by forcing the strategic acquiror to negotiate with the board, while setting a trigger as low as 10 % may be optimal when facing activist investors as they try to exert influence on a company through smaller stakes and are not necessarily seeking ownership of a large block. It is even possible for a company to set the threshold as low as 5 %[66] of outstanding shares, but evidence provides that the lower the threshold, the more likely a Court's scrutiny.

Many shareholder rights plans opted for a 15- 20 % triggering threshold because it ensured stockholders flexibility to acquire a significant number of shares while limiting the risk of any stockholder or group of stockholders acquiring control. Notably, owning more than 15 % would cause a stockholder to be an "interested stockholder" under Delaware's anti-takeover statute[67]. This triggering percentage has prevailed in rights plans for decades on the basis that the Delaware's legislature endorsed it as the threshold that raises a threat sufficient to trigger the state anti-takeover statute. More recently, however, many companies are setting the triggering percentage at 10 %, particularly to address a threat posed by an activist investor who will typically acquire a smaller stake in a company and then use that equity, on its own or with other activist investors, to push for major corporate changes. Activists typically will not seek ownership percentages of 15 % by themselves, but rather combined with other bidders. This peculiar strategy may in principle endanger board's defensive mechanisms as they could acquire control by being undetected, but directors adapted by introducing acting in concert provisions which will thoroughly be investigated afterwards.

For what concerns the primary goal of a poison pill, the Delaware Court of Chancery stated: "the primary purpose of a poison pill is to enable the target board of directors to prevent the acquisition of a majority of the company's stock through an inadequate and/or coercive tender offer"[68]. Moreover, it recognised that the shareholder right plan gives the board "a leverage to negotiate with a would–be acquirer so as to improve the offer as well as the breathing room to explore alternatives to and examine the merits of an unsolicited bid"[69]. This

[66] This threshold is common for a NOL (net operating loss) pill. *See* Gottfried & Donahue *supra* note 19 where they report: "an NOL poison pill is intended to deter any person from acquiring beneficial ownership of 4.99 % or more of the company's common stock without the approval of the company's board of directors". By deterring such acquisitions, NOL poison pills are intended to prevent an "ownership change". "They are aimed at protecting a company's NOLs from being limited or impaired have a lower trigger ownership threshold are not typically as protective of the company as a traditional antitakeover poison pill against an activist investor or group or a hostile suitor if the definition of beneficial ownership strictly tracks the definition of beneficial ownership".
[67] Del. Gen. Corp. Law. § 203.
[68] *In Re Gaylord Container Corp*., 753 A.2d 462, 481 (Del. Ch. 2000).
[69] *Ibidem.*

bright-line reasoning by the Court falls within the boundaries of the second rationale for the adoption of a defensive tactic presented before. In fact, the Court expressly refers to the board's examination process in considering the merits of an unsolicited bid. It has therefore stressed how, in a takeover context, the board has the duty to thoroughly evaluate the bid and explore the alternatives, should it deem the offer received unfair.

Having listed the primary purpose and the components any pill must contain, it is now time to investigate the distinguishing part of any shareholder rights plan to analyse how boards can properly set the defence to contrast a hostile bid. More specifically, address how this type of defensive tactic has evolved since it was introduced to defend against corporate raider T. Boone Pickens[70]. The first prototype of poison pill consisted of an emission of privileged stocks in the form of a dividend to all common stock owners with a 1-to-1 conversion ratio, and it further specified peculiar conditions for its redemption, subordinated to the company's decision. Whenever an acquirer had reached the triggering level (a common threshold was 20 percent), the privileged share owners could have exercised a put option to have their shares bought at the maximum price paid by the bidder. Further, the defensive mechanism was even more effective in a second-step merger scenario[71] – where the bidder aims to acquire control in the first step and then cashes out the remaining shareholders – because the pill operated through a flip-over provision for the remaining shareholders.

Nowadays, the flip-over feature, if triggered, permits the holders of each right to purchase common stocks of the acquiring company at discount, typically at half price, thereby impairing the acquirer's capital structure and drastically diluting the interest of the acquirer's other stockholders[72]. Moreover, when triggered, the right detaches from the stock and trades separately from it, therefore the bidder must deal not only with actual shareholders of the target company, but also with the holders of the right. With respect to the threshold, boards have to take a fundamental decision as the shape of the pill may be drastically altered by their choice; namely they need to consider the trigger upon which the plan begins to have effect. A common feature is to have a two-tier trigger to block hostile bidders from acquiring control while still

[70] *See* Greenwald *supra* note 54.

[71] *See* Bate C. Toms, *Compensating Shareholders Frozen out in Two-Step Mergers*, 78 Col. L. Rev. 548-586, 548 (1979) where he explains how a second step merger operates and the risk for shareholders to be cashed out for an unfair price, or even with junk securities. In fact, in the first step the acquirer aims to get control over the company by means of a tender offer or by private negotiations in the open market, and then it freezes out minority for a price generally equal to the pre-bid share value. The average cost is therefore reduced as the acquirer is permitted to freeze out minority for the intrinsic value of the firm, without paying a control premium

[72] *See* Bainbridge *supra* note 53.

allowing institutional investors to purchase shares[73]. Furthermore, the triggering level also depends on the specific type of transaction.

A pill with only a flip-over provision is vulnerable, though. A classic example of a bidder turning such a pill to its own advantage is Sir James Goldsmith's takeover of Crown Zellerbach[74]. Like most of the first-generation pill, the target's plan only kicked if the bidder sought to effect a freeze-out merger. Therefore, Goldsmith acquired control, but did not squeeze-out the remaining shareholders. Consequently, the acquirer was already in control of the company but did not suffer the dilution the pill was created for. Goldsmith's brilliant decision turned out to be even more detrimental for the target company, as it prevented a favoured bidder (the so-called white knight) from acquiring shares to save the target company. Should it had done so, it would have suffered the pill's poisonous effects and its ownership structure would have been impaired.

Sir James Goldsmith's takeover was a twisting point in the developments of shareholder rights plans because lawyers realised a change was needed and, as anticipated, they opted to introduce a flip-in provision in subsequent pills. The element is typically triggered by the actual acquisition of some specified percentage of the issuer's common stock (again, 20 percent is a commonly used threshold). When triggered, the flip-in pill entitles the holder of each right – except the acquirer and its affiliates or associates – to buy shares of the target issuer's common stock or other securities at half price[75]. An example of bidder's dilution is provided by Pillsbury's shareholder right plan which would have reduced Grand Metropolitan's bid from 85 to 56 %[76].

In addition to the flip-over and flip-in provisions, lawyers apported other subtle adjustments by including specific provisions empowering boards to redeem pills at nominal

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[73] *See* Shirodkar et al. *supra* note 17. In Delaware the validity of a two-tiered pill was upheld by the Delaware Court of Chancery in *Third Point LLC v. Ruprecht*, which imposed a 10 percent trigger threshold on Schedule 13D filers and a 20 percent trigger threshold on Schedule 13G filers.

[74] For a more detailed analysis of the strategy employed *see* Richard D. MacMinn & Douglas O. Cook, *An Anatomy of the Poison Pill*, 12 Managerial and Decision Economics 481-487, 481-482 (1991) where they reported: "The last strategy was the one employed by Sir James Gold- smith in his quest for Crown Zellerbach Corp. Goldsmith capitalized on the fact that the holders of Crown Zellerbach's stock had the right to buy $200 worth of the merged firm's stock for $100 but that these rights were exercisable only if the raider bought 100 % of the company. Goldsmith chose to buy enough shares to ensure majority control but less than the 100 % that would have triggered the rights.8 Applying the antidote allows the raider to realize the dilution benefit but avoid the wealth transfer activated by the rights. It is not surprising that the introduction and rapid popularity of the flip-in provision as an adjunct to the flip-over provision followed on the heels of Goldsmith v. Crown Zellerbach"

[75] *See* Jube Shiver Jr., *Grand Met Agrees to Buy Pillsbury for $5.7 Billion* (1988), Los Angeles Times, https://www.latimes.com/archives/la-xpm-1988-12-19-mn-457-story.html where the whole takeover plan is described. Specifically, it is reported that "a judge struck down key portions of Pillsbury's "poison pill" anti-takeover strategy, which would have made the takeover prohibitively expensive"

[76] *See* Bainbridge *supra* note 53.

costs when allowing desirable acquisitions to go forward. These features are crucial because, as demonstrated, poison pills are double-edged swords and may even be detrimental for a company if not properly used. For instance, it may happen that investors inadvertently trigger the plan – despite being publicised to equity owners – and the poisonous effects are very harmful[77] for the company as a pill, when triggered, issues shares for a considerable percentage of the outstanding capital. Typical redemption provisions include the window provision and the white knight provision. The former endows the board with the ability to redeem the rights for a specified period following the issuance of the pill – therefore augmenting its bargaining power when negotiating with a bidder – and usually lasts 10 days, while the latter was introduced to conclude a transaction approved by the majority of shareholders[78].

There is a vivid debate whether a window provision (commonly known as last look provision) is good for a company. In fact, when a rights plan contains a last look provision, the board is empowered with the final call on whether to hamper bidders' acquisition plans because it has 10 days to redeem the rights after the plan has been triggered. On the one hand, it seems sensible to put this decision in the hands of the board rather than a third party because it has the tools to take an informed decision on such delicate matters; in fact, a triggered rights plan will significantly affect the company and its capital structure. On the other hand, giving the board the final call on whether the dilutive effects occur may weaken the rights plan's deterrent value because during the 10-day window after the plan has been triggered, the board is generally under considerable pressure in deciding whether to redeem the rights and may not take the best decision under those circumstances.

Clearly, this pressure comes from the fact that the board's decision must be consistent with its fiduciary duties – which are owed towards the shareholders rather than towards the company in a takeover scenario – and are based on knowledge of the company's situation, including the "threat" posed by the particular acquiror and the potentially significant effects of the triggered plan. Further, company's stockholders benefiting from the plan may cause

[77] *See* Tim Huber, *Gulp! Buying spree triggers poison pill* (1998), Minneapolis/St. Paul Business Journal, https://www.bizjournals.com/twincities/stories/1998/02/09/story2.html which reports that in 1998 In 1998, Crabbe Huson Group, Inc. inadvertently triggered Arcadia Financial Ltd.'s rights plan, acquiring 16.8% of Arcadia's outstanding shares, which pushed it past the 15% threshold of Arcadia's rights plan. *See also* See Floyd Norris, *Market Place; Investor Says He Bought Stock and Didn't Know It*, The New York Times (2003), https://www.nytimes.com/2003/07/30/business/market-place-investor-says-he-bought-stock-and-didn-t-know-it.html.

[78] The window for redemption however is limited in time, and boards can only do so in the said period. In fact, in the seminal case *Amalgamated Sugar Co. v. NL Industries,* 644 F. Supp. 1229 (S.D.N.Y. 1986) the U.S. District Court rejected a shareholder rights plan because the board had failed to redeem the rights before the acquisition, and they hadn't been redeemed within the time frame.

pressure on the board. Although diluting the acquiror gives the board the chance to increase the ownership percentage at a deeply discounted value (commonly 50 %), the plan, if not redeemed, will likely take the acquiror's proposed deal off the table and boards should be cautious to still be able to maximise shareholder value. Moreover, when a plan is triggered, at least in the takeover context, a significant number of the company's stockholders may be arbitrageurs who had bought company stocks with the expectation that a deal would happen and will likely want the board to redeem the rights and let the acquisition proceed, regardless of the company's long-term interest. Therefore, a board inserting a last look provision in its pill, may signal it is open to negotiate with the potential bidder, and that it may decide to redeem or terminate the rights – thereby reducing the rights plan's deterrent value. In the end, whether or not to include a last look provision is an important issue for a board to consider, and it is key that it will be advised as to the positive and negative implications of the provision.

Another feasible element directors may conceive is the acting in concert provision[79] which is aimed at preventing corporate raiders acting in concert to remain under the threshold individually, but effectively exerting control together. Over the years, especially the past decade, in fact, increased investor activism (particularly hedge fund activism) has given rise to stockholders coordinating their activities in ways not captured by the traditional definition of beneficial ownership. Notably, hedge funds with small stakes in companies (*i.e.,* less than 5 %) coordinating in a way that aggregates to a large block of stock that allows them greater leverage to influence management by effectively exerting control. Hedge funds with the same or similar (often short-term) objective may form a loose network, communicate informally and still pursuing the same strategy. When they act in concert or in parallel to effect change at a company, they may do so without any formal or even tacit agreements and, because there is no actual agreement, arrangement or understanding, their activities will go undetected under a traditional plan.

The adaptive response to protect against this type of stockholder activity, is to embed an "acting in concert" provision in a company's rights plan to broaden the traditional definition of beneficial ownership and capture certain kinds of informal coordination among stockholders. So far, two main types of acting in concert provisions have emerged: an express and a general provision.

[79] *See* Spencer D. Klein et al., *Poison Pill Deep Dive Series: Acting in Concert* (2020), Morrison Foerster.com, https://www.mofo.com/resources/insights/200611-acting-in-concert.html#:~:text=Express%20provision%3A%20Under%20an%20express,is%20%E2%80%9CActing%20in%20Concert.%E2%80%9D.

Under the former, two shareholders are deemed to beneficially own shares together if they are believed to act in concert. Namely, it is provided that a person acts in concert, or in parallel, with another person if such agent knowingly acts (independently of an express agreement, arrangement or understanding) at any time after the first public announcement of the adoption of the shareholder right plan, in concert or in parallel with such other investor. Additionally, they are still deemed to act in concert if they aim at changing or influencing the control of the company together, in connection with or as a participant in any transaction having that purpose or effect. Furthermore, a showing that each person is conscious of the other person(s)' conduct, and at least one additional factor (including exchanging information, attending meetings, conducting discussions, or making or soliciting invitations to act in concert or in parallel) is required. Evidently, an acting in concert provision is not a bright-line standard and the board preserves the discretion as to whether considering two or more investors acting in concert. Given the somewhat blurred dividing-line, a common provision exempts both the making or receiving revocable proxies in response to a public solicitation made to more than ten stockholders of the company, and soliciting or being solicited in connection with a public tender or exchange offer from the acting in parallel definition[80].The general provision, instead, is well suited to address investors acting in concert when an agreement, arrangement or understanding (whether or not in writing) to cooperate in obtaining, changing or influencing control of the company is present.

It is not possible for a shareholder rights plan to embed both the express and the general provision because they both target the same stockholder coordination and, at the origins, acting in parallel provisions required express agreements. According to Professor Guhan Subramanian of Harvard Law School and Harvard Business School[81], the first prototypes of poison pills tracked the definitions of a "group", "affiliate", and "associate" under Section 13(d) and Rule 12b-2 of the Exchange Act. Instead, modern poison pills tend to expand the dimension of "acting in concert" provision (sometimes referred to as a "wolfpack" provision)[82],

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[80] *Ibidem.*

[81] Professor Subramanian is a recognized expert in corporate affairs and has been helpful to this court on many occasions. *In re Starz Appraisal*, 2018 WL 4922095, at *1 (Del. Ch. 2018). His published work concerning policy questions of corporate law fills the footnotes of many decisions of Delaware courts. *See, e.g.*, *In re CNX Gas Corp. S'holder Litig.,* 2010 WL 2291842, at *7 n. 4, *10 n. 5 (Del. Ch. 2010); *In re CNX Gas Corp. S'holder Litig.,* 2010 WL 2705147, at *11 (Del. Ch. 2010); *In re MFW S'holders Litig.,* 67 A.3d 496, 501 n. 3, 530 n. 162 (Del. 2013); *In re Compellent Techs., Inc. S'holder Litig.*, 2011 WL 6382523, at *22 n. 11 (Del. Ch. Dec. 9, 2011); *In re Del Monte Foods Co. S'holders Litig.*, 25 A.3d 813, 840 n. 5, 844 n.6 (Del. Ch. 2011); *In re Cornerstone Therapeutics Inc. S'holder Litig.,* 115 A.3d 1173, 1184 n. 44–45 (Del. 2015).

[82] The phrase "wolfpacks" in this context refers to "a loose association of hedge funds that employs parallel activist strategies toward a target corporation while intentionally avoiding group status under section 13(d)". *See* William

thus giving the board a great amount of latitude for making the AIC determination. If on one side this strengthens the company's defence, on the other side any group of investors may improperly be deemed to act in concert. Furthermore, certain aggressive poison pills may even contain a daisy chain effect where if Party A and Party B are each separately and independently "acting in concert" with Party C, Party A and Party B are deemed to be "acting in concert" with one another[83].

Shareholder rights plans are often litigated and, while Delaware Courts have generally upheld the use of such acting in concert provisions, other courts have not expressly done so. In addition, repeatedly investors harshly criticised the adoption of stringent provisions stating they prevent investors from sharing information. As an example, in the 2017 dispute between the activist investor Carl Icahn and Sandridge Energy, the former defined the defensive provision "patently absurd" and deemed it "a transparent attempt to preclude large shareholders from communicating with one another and exercising their shareholders' rights"[84]. Following to the critique, Sandridge deleted the acting in concert provision, in order to "ensure there is no unintended consequence that might discourage communications between shareholders…"[85]. Similarly, in the 2018 dispute between John Schnatter and Papa John's, the former criticised an express acting in concert provision, alleging that it prevented him from communicating with other stockholders regarding corporate matters such as opposition to board proposals[86].

To conclude, an acting in concert provision should not be drafted in a way that "fundamentally restricts" a successful proxy contest or otherwise prevents stockholders from communicating with each other in a manner otherwise permissible by the law, otherwise it would be too restrictive. Ultimately, companies should consider the facts and circumstances – particularly any actual threats faced – when determining whether to add an acting in concert provision to their rights plans. For instance, if a rights plan is being adopted in response to an actual hostile takeover launched by a strategic acquiror, an acting in concert provision may be unnecessary and may create needless enforceability concerns and even certain dissent among

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R. Tevlin, *The Conscious Parallelism of Wolf Packs: Applying the Antitrust Conspiracy Framework to Section 13(D) Activist Group Formation*, 84 Fordham L. Rev. 2335-2379, 2337 (2016).

[83] *See* Lori Marks-Esterman*, Delaware Chancery Court Invalidates "Anti-Activist" Poison Pill* (2020), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2021/03/16/delaware-chancery-court-invalidates-anti-activist-poison-pill/.

[84] *See* Carl Icahn, *Letter to the Board of Directors of Sandridge Energy* (2017), CarlIcahan.com, https://carlicahn.com/letter-to-the-board-of-directors-of-sandridge-energy/.

[85] *See* Sandridge, Letter to Shareholders (2018), sec.gov, https://www.sec.gov/Archives/edgar/data/1349436/000119312518017581/d511604dex991.html.

[86] *See Schnatter v. Shapiro*, C.A. No. 2018-0646-AGB, (Del. Ch. 2019).

shareholders; however, if a rights plan is being adopted in response to an activist investor, an acting in concert provision may be warranted.

Another peculiar element seldom present in shareholder rights plans is the “qualifying offer” provision[87]. It provides that, if an offer meets certain defined criteria, and the board does not redeem the rights or exempt the offer within a certain period, the stockholders have the right to force the board to call a special meeting to vote on whether to exempt the offer from the rights plan. Differently from the provisions previously described, it empowers shareholders with a strong tool to conclude an acquisition. In fact, once the defence is not in place anymore, the bidder can easily obtain control. Most right plans do not include a qualifying offer provision as, by custom, boards shall have the power to manage the company rather than shareholders. Before adopting it, directors should therefore consider whether, under those circumstances, a qualifying offer provision reduces the board’s leverage by opening a path for an acquiror to sidestep the board and appeal directly to stockholders, whether it could hinder the board’s ability to run an auction process or whether allowing stockholders to vote – in what is essentially a referendum on the offer – could result in an undesirable outcome for the firm. That said, some boards have determined to include the provision to emphasise to stockholders that they are not categorically opposed to a takeover of the company. In fact, both ISS and Glass Lewis state in their guidance for stockholder vote recommendations that rights plans should contain a qualifying offer provision[88].

Although the specifics vary by rights plan, there are some general features an offer would need to satisfy in order to be a “qualifying offer”. Namely, the offer should be for cash, or for common stocks of the offeror (or a combination of both), for all the outstanding common stocks of the company at the same consideration per share. Moreover, the offer needs to exceed the highest market price in the last 12- 24 months (timeframes change on a case-by-case basis). Furter, the offer must remain open for a specified period after any requested special stockholder meeting, and the offeror commits to consummate a second-step merger as soon as possible paying the same consideration to all the remaining shareholders.

[87] It is also commonly known as a “chewable provision”.

[88] *See ISS United States Proxy Voting Guidelines Benchmark Policy Recommendations* (2020), ISS governance.com, https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf. The proxy voting guidelines provide that, when considering whether to recommend that stockholders approve a rights plan that is put to a stockholder vote, the plan should contain a stockholder redemption feature. Specifically, if the board refuses to redeem the rights 90 days after a qualifying offer is announced, 10 % of the shares should be able to call a special meeting or seek a written consent to vote on rescinding the rights. Similarly, *see Glass Lewis 2020 United States Proxy Paper Guidelines*, Glass Lewis.com, https://www.glasslewis.com/wp-ontent/uploads/2016/11/Guidelines_US.pdf.

Once an offer has met the defined criteria, the board has generally between 60 and 90 days to call a meeting. Should the board fail to redeem the rights or exempt the offer from the rights plan within a certain number of days after the offer has commenced, stockholders (exception made for the offeror) holding a specified percentage of the outstanding shares – usually between 10-25 % – may submit a written demand to the board, mandating it to call a special stockholder meeting to vote on the exemption of the offer from the rights plan. After receiving such a demand, a special meeting must be called typically between 90 and 120 days after receipt of the demand. Should the board fail to convene it or should a majority of the outstanding shares (excluding shares held by the offeror) be voted in favour of exempting the offer from the rights plan at the meeting, the offer is deemed exempted from the rights plan, and the consummation of the offer will not trigger the rights plan.

Continuing with the taxonomy, another board's weapon is the grandfather clause. As noted before, nowadays a common feature of capitalism is dispersed ownership, and consequently most companies do not have a control block as each shareholder only owns a small percentage of a company's outstanding shares; however, in certain circumstances, large funds may possess a considerable equity in a company. Therefore, in a takeover scenario, especially when a shareholder right plan entails a low threshold, the poisonous effects may be released as former shareholders already are above the triggering threshold. Evidently, a special provision is needed as to avoid the detrimental effect an improper use of a pill will provoke: the so-called "grandfather clause"[89].

Given that most companies do not have a control block, boards should not embed this special provision in their defensive tactic, but it has become customary to do so as to avoid triggering the rights plan upon adoption if a stockholder has an interest above the threshold prior to the hostile bid. Particularly, given the broad scope of "beneficial ownership" that rights plans entail – beyond what federal securities rules and investors public filings report –, some synthetic interests[90] may be addressed by the beneficial ownership definition and therefore could exceed the threshold level.

In a typical grandfather clause, the following is generally reported: that no person who beneficially owns a certain percentage (15 % usually) or more of the common outstanding

[89] *See* Goodman *supra* note 58.

[90] *See* Shirodkar *supra* note 20 where the article reports that: "certain synthetic interests in securities created by derivative positions—whether or not such interests are considered to be ownership of underlying shares of common stock or are reportable for purposes of Regulation 13D of the Securities Exchange Act of 1934, as amended—are treated as beneficial ownership of the number of shares of common stock equivalent to the economic exposure created by the derivative positions".

shares, at the time of public announcement of the plan, shall be deemed "acquiring person". Additionally, the grandfather stockholders will not be exempt if they drop below the triggering threshold and subsequently exceed the level. Adopting a grandfather clause may seem easy in theory, instead, it requires a meticulous analysis by the board because it has some shortcomings which may lead to the said side effects of a pill. In fact, one of the most recurring questions is: "if a large stockholder is being grandfathered, to what extent should the company take that into account when setting the general triggering threshold?". The matter is even more perilous when an insider is being grandfathered because, should the board miscalculate the equity stake, the pill will then be triggered by an insider and shareholders will most likely remove the board as a consequence of a blatant mistake.

Additionally, it is fair to ask how should founding stockholders and their families be handled. While some plans might consider each family member as a separate stockholder and the threshold level is never exceeded, others will deem all the family members acting in parallel, and the aggregate equity may represent the triggering event. I have previously shown that acting in concert provisions broadly define beneficial ownership; by consequence boards should put maximum care in drafting grandfather provisions so that even considering agreements, arrangements, or understandings (whether or not in writing) suitable to trigger the AIC provision, company's shares do not get diluted. For example, when considering a founding family, if a grandfather shareholder is party to an agreement or arrangement (*e.g.*, an option or derivative contract), at the time of adoption of the pill, pursuant to which the stockholder is deemed beneficial owner of common shares, should the person be able to extend or exercise such agreement at maturity? Or should any change of ownership be considered an acquisition of additional common shares, therefore causing the rights plan to be triggered?

The questions presented are critical for a company and the board's key objective shall be to realise who its significant stockholders are, and the consequences of grandfathering those owners when drafting a poison pill – considered the ease and speed with which shares may be traded, especially in a takeover context. So far, the underlying idea was that grandfather owners do not represent a threat for a company's board and the crucial task for directors was not to suffer the backlash of a poison pill, however it may be the case that former executives wish to win back control. Then, grandfather clauses shall be drafted to block hostile bidders, and at the same time not to damage other block holders[91]. To avoid those dangerous situations, companies

[91] *See* Shan Li, *American Apparel, ousted founder trade power plays* (2014), Los Angeles Times, https://www.latimes.com/business/la-fi-american-apparel-20140701-story.html with the journalist reporting that "the ousted Chief Executive Dov Charney increased his ownership stake before the rights plan triggered (going

should employ an effective stock watch program to detect any conspicuous acquisition and pay attention to rumours in the market. Ultimately, grandfather clauses have to be tailor-made and will reflect the company's stockholder base, the identity and motives of any grandfathered stockholders, and the company's relationship with any grandfathered stockholders.[92]

Shifting the focus to post-bid clauses, a feature worth of citing is the so-called back-end rights plan. It is seldom used and consists in an issuance of privileged shares, debt securities or a mix of both conferred to shareholders depending on their equity stake. The consideration attributed depends on the company's share price at the time of adoption of the pill, rather than on a projected value as it is the case with most poison pills,[93] and the rights are exercisable after a classic triggering event[94]. The main scope of a back-end rights plan is to fix a company's share price and grant all the shareholders to be cashed out for the same consideration[95]. As in most cases, the board still enjoys the redemption provision to assure a desirable acquisition to go forward. Furthermore, target company's directors can employ a dead hand provision to strengthen the back-end plan. In fact, should a bidder acquire control quickly, it could replace management with friendly executives and redeem the plan. By adding a dead hand provision, instead, target boards impede the new board from redeeming the plan – should the acquirer remove a specified percentage of incumbent directors. The effect produced is very similar to the aforementioned staggered board provision.

3. Effects on the company and directors' careers

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from 27 % to 43 % ownership) and the retailer's board maneuvered to block him from retaking control". By consequence, the board had to face its former CEO – which was by far its biggest stockholder – and adopted the defensive tactic (containing a grandfather clause) to delay the time for the share acquisition.

[92] *See* Goodman *supra* note 58.

[93] However, *see Dynamics Corp. of America v. CTS Corp.*, 635 F. Supp. 1174 (N.D. Ill. 1986), where the court upheld a back-end rights plan where the price depended on the projected value the company could realise throughout the duration of the plan (12 months).

[94] For a more in-depth analysis *see* Martin Lipton & Andrew R. Brownstein, *Takeover responses: an update, dynamics of corporate control II,* 40 The business lawyer 1403-1430, 1403-1405 (1985). The stocks issued in a back-end right plan can be conceived so that the acquirer cannot render them worthless. Typical clauses include limitations not to increase company's leverage, or not to sell the company or to abide by previous board resolutions concerning a company's liquidity. Back-end rights plans allow its holders to exchange common stocks for company's debt instruments, rather than allowing them to purchase additional stocks at a favourable price. Secondly, the value of stocks issuance and the conversion ratio is calculated by the board based on the current value at the time of adoption of the plan. Finally, the right to exchange commons stocks for debt securities is limited in time.

[95]*Id.* at 1417. The article points out: "how Houston Natural Gas Corporation combined a self-tender for approximately 19 % of its shares (with the right to increase to approximately 26 %) at $69 per share with a counter tender offer in order to defend against the front-end loaded two-tier offer for Houston Natural made by Coastal Corporation pursuant to which Coastal sought to acquire approximately 45 % of Houston Natural's shares at $68 per share and then squeeze out the remaining shareholders for unspecified securities having a value of less than $68 per share".

The analysis of the different ad hoc provisions board may adopt has provided a thorough overview of how poison pills help directors in negotiating a higher price. However ever since they have been introduced by Martin Lipton, there has been a long debate regarding the effective benefits and downsides shareholder rights plan may apport to companies. These disputes contribute to the never-ending conflict of interest between directors and shareholders which has resulted in three opposite views for the adoption of a poison pill: the entrenchment, the shareholders' interest and the neutral one[96]. The first holds that shareholder rights plans entrench managers at stockholders' expense. Further it posits that directors adopting a pill face the risk of shareholder backlash and negative career consequences[97]. At the opposite side of the spectrum, the second view sustains that poison pills improve the firm's operations, increase expected takeover premiums; it implies that directors deploying shareholder rights plans are valuable to stockholders and should enjoy career benefits. The last one believes that the explicit adoption of a poison pill has little impact, either because most companies already have latent defensive measures or because the market does not strongly react to directors' actions. Obviously the first and the second views are the most popular due to the disruptive nature of the poison pills which has caused people to take sides.

The entrenchment view believes that shareholder rights plans negatively affect companies and, especially when takeover defences are sticky and costly to remove, the relation between firm value and the use of anti-takeover mechanisms declines (eventually becoming negative) as the firm ages[98]. This is also known as the value reversal theory as there is a threshold (around 5 years from the incorporation date) where the downsides start to outweigh the benefits[99]. The implied reasoning is that net benefits of shareholder rights plans (such as guarantees against changes in corporate strategies which can guide the firm throughout its early stages) sharply decrease as firms age while costs of entrenchment increase making them less

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[96] *See* William C. Johnson et al., *The Consequences to Directors of Deploying Poison Pills*, Fisher College of Business WP 2019-03-023, *available at* https://ssrn.com/abstract=3460201.

[97] *Id.*

[98] *See* William C. Johnson et al., *The Lifecycle Effects of Corporate Takeover Defenses*, ECGI Finance Working Paper N° 761/2021, http://ssrn.com/abstract_id=2808208. In their own words: "We hypothesize that two forces drive the value reversal pattern. Firstly, takeover defences convey fewer benefits and impose higher costs as a firm ages. The second force that drives the value reversal is that takeover defences are extremely sticky, *i.e.,* firms do not frequently remove them. If takeover defences were not sticky, firms would adjust their defences as the benefits decrease and costs increase, and there would be no value reversal". Particularly, they demonstrate how this relationship holds by analysing a large sample of going public U.S. companies and showing that the value reversal is driven mostly by the defences adopted at the IPO rather than the ones added during the course of action: this is due to the fact that the formers are the strongest and hardest to repeal, causing costs to exceed benefits as they are not removed.

[99] *Id.* at *24.

appetible.[100] As a consequence of the adoption of a plan, directors may be subject to negative career repercussions connected to a reputational loss[101]. In fact, directors labour market seems very sensible especially to first-time adopters (managers who adopt poison pills for the first time) when they approve the plan. Directors mainly suffer lower vote support in subsequent board elections, a higher likelihood to leave the boards on which they currently serve, and a lower probability to be appointed as new directors at other firms.

A completely different view is the shareholder's interest. Proponents believe shareholders rights plans are beneficial to the company. Specifically, shadow pills – which are deployed without shareholder's approval – are valuable for corporations mainly because they limit shareholders' ability to harness firm's long-term strategy and serve as a commitment device that binds the shareholders to the firm's current long-term strategy and to a cooperative relationship with the board. Notably, when a defensive tactic is in place, longer-term and firm-specific investment projects by its stakeholder are protected and the costs of contracting are reduced. Such commitment is especially valuable for firms with large share of intangible assets, that are more subject to asymmetric information and hence may be undervalued by outsiders[102]. Another founding element of this view is the "bargaining power hypothesis" which sustains that having the right to adopt a poison pill strengthens the negotiating position of the board vis-à-vis any potential bidder, allowing directors to obtain a higher offering price for the target's shareholders[103].

A conflict among these views emerges in the relation between the deployment of the pills and innovation inside the company: a key aspect managers should consider when choosing a shareholder right plan. There are in fact two contrasting opinions backed by either one of the two views: the agency theory and the "play it safe" theory[104]. The former posits that low external monitoring increases the room for managerial moral hazard, whilst the latter argues that too much pressure from the market for corporate control and myopic shareholders may

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[100] *Id.* at *26.
[101] *See* Martijn Cremers et al., *Shadow Pills, Visible Pill Policy, and Firm Value*, ECGI Finance Working Paper N° 595/2019, http://ssrn.com/abstract_id=3074658 as they argue that directors, and boards in their entirety, may suffer s legal challenges and/or reputational harm of being viewed as a "pro-pill" board.
[102] *Id.* at * 6 the so-called "commitment hypothesis".
[103] *Ibidem.* at * 6.
[104] *See* William Mbanyele, *Staggered Boards, Unequal Voting Rights, Poison Pills and Innovation Intensity: New Evidence from the Asian Markets,* International Review of Law and Economics (forthcoming), *available at:* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3743318. The theory proposes that "insulating managers from takeover threats can alleviate myopic behaviour exacerbated by the market for corporate control due to pricing inefficiencies of intangible assets. Due to market imperfections, investors can not accurately evaluate long-term innovative projects' value, resulting in undervaluation of innovative companies and exposure to opportunistic bidders". Therefore, directors should be protected from these threats and allowed to choose what is best for the company.

encourage a quiet life for managers.[105]. Departing from these diverging views, a question is commonly raised: "what should be the board's primary goal in a takeover context?" and consequently: "what are the boundaries for its actions?". To provide an answer, it is key to investigate historical U.S. courts decisions and examine the standards directors need to abide by to avoid liability.

III. PEACE AFTER THE STORM. DELAWARE'S STANDARD OF REVIEW

A. Unocal, Moran *and* Revlon

As above mentioned, during the 1980s and 1990s' takeover waves[106], in response to the acquisition strategies usually consisting of a round-up and subsequent takeover bid model, the target companies developed a heterogeneous variety of defensive tactics, both pre-bid and post-bid. Delaware courts tried to set a standard aimed at balancing the company's interest and the boards' artifices that result in board entrenchment. In fact, given the regulation by litigation model in place in the U.S., both Chancery and Supreme Courts are responsible for drawing the line between legitimate actions to protect stockholders and thwart coercive offers, and illegitimate abuses aimed at entrenching the board, therefore breaching the fiduciary duties. However, the task assigned to those courts is rather difficult as the market for corporate control has been a warfare (especially in the last two decades of the past Century) and directors have employed ever-evolving defensive measures to respond to those threats. Despite the convoluted scenario, an overview of the key decisions is crucial to understand how courts outlined the current standard and speculate over future applications of the pill.

The analysis of historical decisions starts from *Pogostin v. Rice* where the Delaware Supreme Court has expressly stated it would use the business judgement rule as the standard of review. The Court had reported[107] the business judgment rule was "equally applicable [...] in the context of a takeover". The lax approach was harshly criticised and the court in *Smith v. Van Gorkom*[108] already disapplied it only a year later, in 1985, in a Supreme Court decision on

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[105] *Id.* at *4.

[106] *See* D. J Block & Y. Miller, *The Responsibilities and Obligations of Corporate Directors in Takeover Contests,* 11 Sec. Reg. L. J. 44, 44 (1983) where they reported that the number of hostile tender offers was "virtually without precedents".

[107] *Pogostin v. Rice* 480 A. 2d 619 (Del. 1984).

[108] In a class action against defendant Trans Union Corporation ("Trans Union") and its board of directors, plaintiffs, who are shareholders of Trans Union, claimed that the approval of the cash-out merger of their corporation violated Del. Code Ann. tit. 8, § 251, and did not warrant business judgment rule protection because the decision was uninformed. Defendant Jerome W. Van Gorkom, Chairman and CEO of Trans Union struck the deal with Jay A. Pritzker. The former successfully convinced the board of the $55 price per share cash-out merger.

an uninformed decision take by the board where it refused to apply the BJR to scrutinise board's actions. The subsequent decision in *Unocal v. Mesa Petroleum Co*[109] set the standard to second-guess board's defensive tactics. Firstly, the Court rejected plaintiff's claim that directors had coercively blocked Mesa's tender offer by stating that it had the "duty to oppose a bid it perceived to be harmful to the corporate enterprise"[110]. The court went on to reason that Mesa was known to be a "greenmailer"[111] and that the offer was coercive. Therefore, it affirmed the "board's duty to protect the corporate enterprise, which includes the other shareholders, from threatened harm"[112]. Secondly, it stressed it would not substitute its views for those of the board if they could be attributed to any "rational business purpose"[113]. Finally, it introduced an enhanced scrutiny which became famous as the *Unocal* two-prong standard. It posed the burden of proving that they had "reasonable grounds for believing that a danger to corporate policy and effectiveness existed because of another person's stock ownership"[114] and that the defensive measure was "reasonable in relation to the threat posed" on directors.

The Court's decision is in between the *Pogostin v. Rice* and *Smith v. Van Gorkom* as it allowed directors' defensive tactics to be shielded by the most deferential standard (the business judgment rule) but, at the same time, posed a higher requirement on directors. The rationale behind the Court's reasoning is that applying a simple business judgement rule could incentivise boards to deploy defensive mechanisms of any type, therefore causing board entrenchment and disserving the shareholder value. Notably, the Supreme Court acknowledged

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The price however was merely assumed by Van Gorkom and was not supported by any valuation information. Following trial, the former Chancellor erroneously granted judgment for the defendant directors and deemed the board informed when taking the decision. The Supreme Court reversed in 488 A.2d 858 (Del. 1985), and underlined directors were grossly negligent in permitting the agreement to be amended in a way they had not authorized. Moreover, it stated that directors had breached their fiduciary duty to their stockholders by failing to inform themselves and by failing to disclose all material information to the stockholders for their approval.

[109] 493 A.2d 946 (Del. 1985). Mesa was the owner of approximately 13 % Unocal's stocks and commenced a two-tier cash tender offer to increase its equity up to 37 % for $ 54 a share. Mesa would have attempted to squeeze out the remaining shareholders with an inequitable consideration. The board was advised to employ a self-tender offer at $72 per stock – which truly reflected the company's value –, should the acquirer had continued with its coercive plan. The Court upheld Unocal's decision to prevent Mesa from benefiting from the offer and reasoned it would have not second-guessed the decision. The business judgement rule was therefore affirmed for the case at stake.

[110] *Id.* at 947. A long list of legal precedents prescribes boards to act whenever a threat to the company is posed. *See e.g. Panter v. Marshall Field Co.*, 646 F.2d 271, 297 (7th Cir. 1981); *Crouse-Hinds Co. v. Internorth, Inc.*, 634 F.2d 690, 704 (2d Cir. 1980); *Heit v. Baird*, 567 F.2d 1157, 1161 (1st Cir. 1977); *Cheff v. Mathes*, 199 A.2d at 56; *Martin v. American Potash Chemical Corp.,* 92 A.2d at 302; *Kaplan v. Goldsamt*, 380 A.2d at 568-69; *Kors v. Carey*, 158 A.2d at 141; *Northwest Industries*, *Inc. v. B.F. Goodrich Co.*, 301 F.Supp. 706, 712 (M.D.Ill. 1969).

[111] *Id.* at 956. The term "greenmail" refers to the practice of buying out a takeover bidder's stock at a premium that is not available to other shareholders in order to prevent the takeover.

[112] *Id.* at 958.

[113] The Court here cited the decision in *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971).

[114] *See Unocal* at 955.

the "omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders"[115]. Given that the standard set in *Unocal* has provided a quick, fair and straightforward way to scrutinise board's decisions in takeover context, it has ruled over the matter ever since.

The subsequent decision in *Moran v. Household Int'l, Inc*[116] was the first where a pre-bid shareholder rights plan adopted in response to a takeover[117] was upheld by a Court. Responding to the appellants' first contention that the board lacked authority to act, the Court rejected the claim by showing it had authority to employ the rights plan – pursuant to the DGCL[118] –, and therefore opined the board's defensive mechanism enjoyed the protection of the business judgment rule. The Court's response to this allegation was peculiar because it underlined how, in a regulation by litigation model, the law adapts to situations and merely alleging there are no legal precedents cannot authorise a board to act, standing alone[119].

Further, the Court rejected appellants' second claim that the plan usurped stockholders' rights to receive tender offers by changing the company's fundamental structure. Namely, the Supreme Court affirmed the Chancery Court's opinion that the rights plan did not limit the voting power of individual shares and that the defensive tactic did not impair the ownership structure, differently from other unconventional measures[120]. The Court's approach was to list some possible ways through which shareholders could still be the recipient of a proxy campaign and concluded "the rights plan does not prevent stockholders from receiving tender offers"[121].

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[115] *Id.* at 954.

[116] *Moran v. Household International, Inc.,* 490 A.2d 1059 (Del Ch. 1985) *aff'd*, 500 A.2d 1346 (Del. 1985).

[117] The plan consisted of a two-tier antitakeover provision aimed at defending the company from a hostile bidder. The board set two thresholds (the announcement of a tender offer for 30 percent of Household's shares ("30 % trigger") and the acquisition of 20 percent of Household's shares by any single entity or group ("20 % trigger") for the rights to become exercisable. In particular, the rights were issued and immediately exercisable to "purchase 1/100 share of new preferred stock for $100 and were redeemable by the Board for $ 0.50 per Right. If 20 percent of Household's shares was acquired by anyone, the Rights were issued, became non-redeemable and were exercisable to purchase 1/100 of a share of preferred. If a Right was not exercised for preferred, and thereafter, a merger or consolidation occurred, the Rights holder could exercise each Right to purchase $200 of the common stock of the tender offeror for $100".

[118] The Court expressly cited the Title 8 of the Delaware General Corporate Law § 141(a) and noted the statute vests the board with the power to manage the business and affairs of the company. Additionally, the Court cited the decision in *Unocal* where the same analysis was carried forward; similarly, the Court ascertained the board had authority to act.

[119] In particular, the complainant sustained § 157 has never served the purpose of authorising a takeover defence by only noting there were no legal precedents for it. However, they failed to show the provision forbade directors from adopting the plan.

[120] *See e.g*., *Whittaker Corp. v. Edgar,* 535 F. Supp. 933 (N.D. Ill. 1982), *Cheff v. Mathes,* 199 A.2d 548 (Del. 1964), *Unocal Corp. v. Mesa Petroleum Co., supra* note 109.

[121] *See Moran* at 1354. Some of the ways the Court identified to receive a tender offer are (i) "tendering with a condition that the Board redeem the Rights, or (ii) tendering with a high minimum condition of shares and Rights, or even (iii) tendering and soliciting consents to remove the Board and redeem the Rights. Or even (iv) acquiring 50 % of the shares and causing Household to self-tender for the Rights. Lastly, (v) one could also form a group of up to 19.9 % and solicit proxies for consents to remove the Board and redeem the Rights".

Lastly, claimants contended that the board was unauthorised to restrict stockholders' rights to receive a proxy contest[122]. And the Court rejected this claim too. What stems from this case is that, so long as stockholders' choice is not unique, the poison pill is not preclusive and therefore will be upheld by a Court.

Another seminal decision in takeover contexts is the paradigmatic *Revlon, Inc. v. MacAndrews & Forbes Holding, Inc*[123]. It is the leading case for change of control and essentially constrained boards' actions when it is clear the company is on sale. In its own words, the Supreme Court put: "the directors' role changes from defenders of the corporate bastion to auctioneers charged with getting the best price"[124]. To sum up, the Revlon's board rejected Pantry Pride's friendly offer[125] for an inadequate price; it therefore put in place numerous defensive measures – a shareholder rights plan, an asset repurchases and a lock-up agreement. The target's board negotiated its sale with another company[126] and opted to accept the latter offer, despite inferior. The Chancery Court upheld the use of the rights plan[127], but recognised the board breached the duty of loyalty[128] (by discretionally preferring one bidder over the other) and therefore by failing to maximise the shareholder value (*i.e.,* negotiation price). The Supreme Court affirmed it.

The *Revlon* decision might be deemed problematic for two main reasons: did it establish special duties to govern control auctions or were the so-called *"Revlon duties"* really just the general *Unocal* rules applied to a specific fact situation? The Supreme Court responded to this

[122] A viable, yet costly way to complete a takeover is through an acquisition of a sensible equity in the company (*e.g.,* 10 %) and then conduct a proxy contest to vote against the directors, thereby replacing the board. *See* Bainbridge *supra* note 38 § 12.6 where he posited: "proxy contest long has been the most expensive, the most uncertain and the least used of the various techniques for acquiring corporate control". The main factors are shareholders apathy – specifically the belief proxy insurgents are not serious contenders for control – and the low level of confidentiality it entails as incumbents receive the info of the proxy campaign too.
[123] 506 A.2d 173 (Del. 1986).
[124] *Revlon*, 506 A.2d at 178.
[125] Pantry Pride's CEO attempted to strike a deal with Revlon's CEO for a too low consideration ($ 40 per share). The offer was correctly rejected. To negotiate a higher price, the target's board was advised to both repurchase a considerable amount of its own shares ($ 5 million) and issue a Note Rights plan which consisted in an issuance of debt securities entitling the holders to exchange one common share for a $ 65 principal Revlon note at 12 % interest with a one-year maturity.
[126] Once the friendly purchase was rejected and the acquirer proposed a second higher offer, a bid contest between Pantry Pride and the preferred acquirer (Forstmann) started. The board favoured the second bidder for 3 main reasons: (i) the offeror would provide conspicuous benefits to managers through a golden parachute (termination agreements providing substantial bonuses and other benefits for managers and certain directors upon a change in control of a company) and (ii) Revlon's CEO personal aversion towards Pantry Pride's (iii) and it protected the noteholders.
[127] In fact, the Court stated the board had power to act. It adopted the defensive tactic following to a perceived threat; additionally, it redeemed to allow the second offer to go forward and therefore it was unnecessary to further inquire on the second *Unocal* prong (the reasonableness of the response).
[128] Turning to the lock-up arrangement, the Court opined that Revlon board's justification it adopted the plan to protect its noteholders was irrelevant (as at that point the main board's duty was to protect equity holders), and by selectively choosing the second bidder it had not served the shareholder value.

question in a subsequent decision in 1987[129] where it drew a sharp distinction between the two standards. Later, in 1989 it indicated *Revlon* is "merely one of an unbroken line of cases that seek to prevent the conflicts of interest that arise in the field of M&A"[130]. The question boils down to the evident differences arising from the two cases. Further, an even more problematic point is to determine when directors' duties switched from being "defenders of the corporate bastion"[131] to "auctioneers". With the benefit of hindsight, their role drastically changed from defending the corporate from the hostile bidders to negotiating the highest price, and it happened when the company made clear it was for sale; however, directors perform a quite difficult task by suddenly adapting their strategy towards the new goal. The answers to these questions will be provided by the following decisions in the *Paramount* cases and in the subsequent *Unitrin* case.

B. Rebalancing the Unocal *and* Revlon *standards: from* Paramount *to* Third Point

Once the two milestones upon which courts rely when scrutinising boards' actions in takeover contexts had been introduced, in the subsequent cases, Delaware courts adapted the theoretical standards to practical examples. The task was quite challenging because the dividing line between permissible and impermissible boards' actions is blurred. The analysis now delves into the duo of *Paramount* cases which shed the light on the applicability of *Revlon* in change of control transactions. The two subsequent decisions are: *Paramount v. Time*[132] where the Court recognised *Revlon's* duties had not triggered, and *Paramount v. QVC*[133] where the Court rejected the former's reading and stated *Revlon* had triggered.

In the first case, The Time board began to consider joint ventures with other companies pursuing its long- term goal of expanding into the global market. It initiated merger discussions and eventually established a merger agreement with Warner Communication[134] in pursuit of its long-term strategic plan. However, shortly before Time' s shareholders were to vote on the

[129] *Ivanhoe Partners v. Newmont Mining Corp.*, 535 A.2d 1334 (Del. 1987).
[130] *Barkan v. Amsted Industries, Inc.*, 567 A.2d 1279, 1286 (Del.1989).
[131] *See Revlon* at 182.
[132] *Paramount Communications, Inc. v. Time Inc.,* 571 A.2d 1140 (Del. 1989).
[133] *Paramount Communications v. QVC Network Inc.,* 637 A.2d 34 (Del. 1994).
[134] The plan was structured as follows: (i) Former Warner shareholders would receive newly issued Time shares representing approximately 62 % of the shares of the combined entity. (ii) A Lockup Option – was present "to discourage any effort to upset the transaction", giving each party the option to trigger an exchange of shares. Finally, (iii) a no shop clause supplemented the plan by obtaining commitments from various banks that they would not finance a takeover bid from Time.

merger agreement, Paramount made a cash tender offer for Time; the target board rejected it as inadequate, and Time and Warner's boards agreed on a new plan to forestall Paramount[135.] In evaluating board's decisions, the Supreme Court first asserted that Time's decision to merge with Warner enjoyed the protection of the business judgement rule. It further noted *Revlon's* duties had not triggered because control of the entity "existed in a fluid aggregation of unaffiliated shareholders representing a voting majority – in other words, in the market"[136]. The decision was blatantly wrong and, in Professor Bainbridge's own words, Time's interpretation of *Revlon*, is in the "dust bin of history"[137].

The Court clarified when *Revlon* triggers, which is both when "a corporation initiates an active bidding process seeking to sell itself or to effect a business reorganisation involving a clear break-up of the company"[138], and when "in response to a bidder's offer, a target abandons its long-term strategy and seeks an alternative transaction involving the breakup of the company"[139]. The decision seems to be offering an unmistakable test to clarify when *Revlon* triggers, but it was fundamentally wrong.

The second *Paramount* case[140] offered a divergent perspective on when *Revlon's* duties trigger. In fact, the Chancery Court found that, despite Paramount had not initiated an active bidding process nor abandoned its long-term strategy, *Revlon*'s duties had triggered. The doctrinal shift occurred due to the potential conflict of interest arising in transactions alike. The rationale is that deploying aggressive defensive tactics of any type thereby precluding shareholders from voting on the merger agreement reasonably might lead one to infer directors were acting in their own selfish interest. Therefore, an enhanced scrutiny is needed to rule over those complex situations. The decision served three main purposes: (i) it cured the previous decision's fallacies and reintroduced a fair application of *Revlon*'s duties, (ii) it restored the pre-*Time* view that *Revlon* and *Unocal* are part of the same line of cases in which the significant

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[135] Time would have made a cash tender offer for a majority block of Warner shares to be followed by a merger in which remaining Warner shares would have been acquired, thus obviating the need for shareholder approval. The new agreement would have caused Time to incur between 7 and 10 billion dollars in additional debt as opposed to the old plan and Time's shareholders would have ended up as minority shareholders in a company saddled with substantial debt and whose stock price almost certainly would have been deflated in the short run than the Paramount offer.
[136] *See supra* note 132 at 1150.
[137] *See* Bainbridge *supra* note 35 § 12.9.
[138] *See e.g., Mills Acquisition Co. v. Macmillan, Inc*., 559 A.2d 1261 (Del. 1988).
[139] *See supra* note 132 at 1150.
[140] *See supra* note 133. In short, Paramount entered merger discussions with Viacom, and they sought to preclude other bidders from entering the deal through lockups and no shop clauses. QVC presented a competing bid, nevertheless Paramount's board recommended the first offer relying on *Time*'s reading of *Revlon.* The Court rejected Paramount's claim and restored the pre-*Time* reading of *Revlon* reasoning an enhanced duty is required when directors' actions may lead one to reasonably infer they were acting in their own interests.

conflict of interest found in certain control transactions justified enhanced judicial scrutiny, and (iii) it made clear that, so long as the board's conduct falls within the bounds of reasonableness, Delaware courts will not second-guess board's decisions.

Delaware's restraint from second-guessing board's decisions was confirmed in unmistakable terms by the subsequent decision in *Unitrin, Inc. v. American General Corp.*[141] where the Supreme Court, rejecting the Chancery Court's reading, focused on the possibility for the board of being replaced. It further concluded, the decision to deploy defensive mechanisms does not in principle entail a conflicted transactions when the shareholders can oust directors[142]. Stemming from that, a defence is disproportionate only when "coercive" or "preclusive". Absent such characteristic, boards' decisions are generally protected by the business judgement rule rather than by a more stringent standard as the "substantive reasonableness review" (or enhanced scrutiny)[143]. To sum up, the *Unitrin* standard prescribes a defensive tactic to be inadmissible only if "coercive" or "preclusive" – because adverse to shareholders' interests – while allowing any type of defensive tactic so long as it is redeemable[144].

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[141] *Unitrin, Inc. v. American General Corp.,* 651 A.2d 1361 (Del. 1995).

[142] *Unitrin* boils down to not considering a defensive tactic "preclusive" so long as shareholders' vote is still available. The Delaware Court of Chancery upheld both a shareholder rights plan and an amendment to the bylaws so to embed certain shark repellent measures but deemed "unnecessary" – because unreasonable under *Unocal* – a stock repurchase. The Supreme Court reversed and outlined how the Chancery Court "erred in holding that the adoption of the Repurchase Program would materially affect the ability of an insurgent stockholder to win a proxy contest". In fact, the Chancellor had erroneously substituted its judgement to the board's. The Supreme Court went on to list why the board rationally perceived the threat from the American General's offer to be a form of substantive coercion. It highlighted "the Board noted that Unitrin's stock price had moved up, on higher than normal trading volume" or that "some Unitrin shareholders had publicly expressed interest in selling at or near the price in the Offer" (they are both two clear signs a takeover was on the verge of coming). Moreover, it sustained the board's decision to operate a stock repurchase in view of the deflated price at which it was trading and consequently, "that the board considered Unitrin stock to be a good long-term investment".

[143] In one of its passages, the Court explained "the ratio decidendi for the "range of reasonableness" standard is a need of the board of the directors for latitude in discharging its fiduciary duties to the corporation and its shareholders when defending against perceived threats. The concomitant requirement is for judicial restraint. Consequently, if the board of directors' defensive response is not draconian (preclusive or coercive) and is within a "range of reasonableness", a court must not substitute its judgement for the board's". The Court therefore focused on the availability of an instrument for shareholders to replace management; more specifically, whether this substitution "would either be mathematically impossible or realistically unattainable". Additionally, it broadened the admissibility of a poison pill considering the "substantive coercion" as a "*Unocal* qualifying threat" (*Unitrin*, 1388-89).

[144] The decision in *Unitrin* left many questions open. *See* Jeffrey N. Gordon, *Just Say Never? Poison Pills, Deadhand Pills, and Shareholder-Adopted Bylaws: An Essay for Warren Buffett*, 19 Card. L. Rev. 511, 511 (1997) where the main concerns are (i) "whether a board can "just say no" to a hostile bid, (ii) whether a board can thwart a proxy fight to redeem a poison pill through a "continuing director" provision in its pill (what might be called "just say never") and (iii) whether shareholders can use their power to amend bylaws to constrain the adoption and maintenance of a pill". He further noted that, while on one side a board's refusal to redeem a poison pill may be considered "preclusive" – as the decision is not subject to a shareholder vote – on the other side, citing *Moran*, should directors be "displeased with the action of their elected representatives, the power of corporate democracy is at their disposal to turn the board out".

Another noteworthy legal precedent in Delaware case law is represented by its 2010 Chancery Court decision in *Selectica Inc. v. Versata Enters. Inc,* later affirmed on appeal by the Supreme Court[145] too. The target company's directors (Selectica) reduced the trigger of their shareholder rights plan from 15 % to 4.99 % to protect their NOLs[146],in light of a perceived takeover threat from Versata Enterprises. Moreover, the board capped existing shareholders who held a 5 % or more interest to a further increase of only 0.5 %.

Turning to the Supreme Court's analysis, it first rejected plaintiff's claim that the Chancery Court erred in applying the *Unocal* standard of review and then affirmed its lower court's decision that the poison pill was not preclusive. For what concerns the first prong, the Supreme Court found that directors satisfied the requirements by showing they had "reasonable grounds for believing that a danger to corporate policy and effectiveness existed because of another person's stock ownership"[147]. The Court further noted that the bidder's purpose was to "intentionally impair corporate assets"[148] – thereby coercing the board into meeting certain business demand under the threat of impairment – rather than conducting a hostile takeover. Consequently, the threat was present.

For the second prong, (*i.e.,* the proportionality of the response) the Court outlined the *Unocal* test is context-specific and board's evaluation is necessary to thwart hostile bids, while serving the shareholder value at the same time. It determined the defensive measure was a proportionate response to the stock acquisition, supported by the record and resulting from a "logical deductive reasoning process"[149]. The rationale is that the defence did not preclude a proxy contest, and therefore it was not coercive. In its reasoning the Court explicitly referred to *Unocal* stating the decision was "reasonable in relation to the threat identified"[150].

Despite this pro-director decision, the Court insisted it upheld the pill, having considered the specific scenario. In fact, it realised companies could rely on the Court's reasoning and reinterpret it at their own advantage. For this purpose, it stressed the decision "shall not be construed as generally approving the reasonableness of a 4.99 % trigger in the Rights Plan of

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[145] 5 A.3d 586 (Del. 2010).

[146] The Court defined the net operating losses as follows: "they are tax losses, realized and accumulated by a corporation, that can be used to shelter future (or immediate past) income from taxation".

[147] *Id.* at 601. The board in fact held numerous meetings and was properly advised to defend the corporate asset (the most valuable it had, given the downward path the company was following). Therefore, when the bidder surpassed the threshold limit, the poison pill triggered and reduced its common stock ownership by 50 % (from 6.7 % to 3.3 %).

[148] *Id.* at 606.

[149] *Id.* at 601.

[150] *See Unocal supra* note 109 at 955.

a corporation with or without NOLs"[151]. *Selectica* demonstrated once more the flexibility of Delaware corporate law suggesting that independent directors acting on good faith, on an informed basis and properly advised by experts, are given substantial freedom in deciding what is best for the company. It also proved specifically how the poison pill remains a flexible tool for boards of Delaware corporations[152].

Few months later, the Delaware Chancery Court issued another seminal decision in *Airgas, Inc. v. Air Products and Chemicals, Inc*[153] which delved into the everlasting dilemma concerning the delegation of corporate powers from shareholders to directors. In particular, it answered to the question whether a fully informed board (fulfilling the predetermined standards of acting in good faith, once a reasonable threat has been identified and employing a defensive tactic – a poison pill in the said scenario – that falls within the boundaries of reasonableness) can prevent the stockholders from taking their own decision, and if a board can "just say never"[154] to a hostile tender offer. The Court firmly denied boards from essentially dismissing any type of hostile tender offer – because, should it have done so, boards' rejection would have not been subject to review anymore – but highlighted Delaware' well-known reputation of "director primacy state". In fact, it sustained that "the power lies with the board of directors"[155].

In its decision, the Chancellor reported the poison pill served its main purpose – increasing the offering price quite a lot[156] and slowing the acquisition process –, but also stated that in his opinion the "inadequate price" for an all-cash non-coercive bid does not in principle preclude a Court from applying a standard stricter than the *Unocal*. Nevertheless, he ascertained that in previous decisions inadequate price was recognised as a valid threat to corporate policy and effectiveness[157], that the "selection of a time frame for achievement of corporate goals . . . may not be delegated to the stockholders"[158]; therefore he upheld the pill.

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[151] *Id.* at 607. It also cited *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d at 1378 (citing *Moran v. Household Int'l, Inc.*, 500 A.2d at 1355 and *Revlon, Inc. v. MacAndrews Forbes Holdings, Inc.*, 506 A.2d 173, 179 (Del. 1986)).
[152] *See* Mark D. Gerstein, *Implications of* Selectica *for Next-Generation Poison Pills* (2010), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2010/03/30/implications-of-selectica-for-next-generation-poison-pills/.
[153] 16 A .3d 48 (Del. Ch. 2010).
[154] The question, arising from the *Unitrin* decision is extensively treated by Jeffrey N. Gordon in *Just Say Never? Poison Pills, Deadhand Pills, and Shareholder-Adopted Bylaws: An Essay for Warren Buffett*. *See supra* note 144.
[155] *See Airgas* at 55.
[156] *Id.* at 57 "it has helped the Airgas board push Air Products to raise its bid by $10 per share from when it was first publicly announced to what Air Products has now represented is its highest offer".
[157] *See Unitrin* at 1384: "This Court has held that the 'inadequate value' of an all cash for all shares offer is a 'legally cognizable threat.'", quoting *Paramount,* 571 A.2d at 1153.
[158] *Paramount*, 571 A.2d at 1154.

Even more recently, a Delaware Chancery Court decision – *Third Point LLC v. Ruprecht, C.A.*[159] – has confirmed the applicability of the *Unocal* standard with respect to shareholder rights plans; stressing that director's actions are not to be halted should the pill be compliant with the 2-prong test and non-coercive[160]. In particular, the board adopted a one-year two-tier poison pill[161] sustained by a "qualifying offer" provision[162]. The plaintiffs hedge fund and institutional investors sought to enjoin the plan, but the Court found them unable to satisfy the three necessary prongs[163]. Turning to the plan's analysis, the Court found directors acting in good faith[164]. Secondly, it concluded Third Point's offer represented a cognizable threat for the company, and thirdly the shareholder rights plan was a reasonable response. Finally, the denial to plaintiffs' request to waive the 10 % trigger was within the range of reasonableness and the Chancellor did not grant an injunction because plaintiff failed to show the proxy contest was "realistically unattainable"[165]. Again, the Court concluded that, so long as a board employs a shareholder rights plan adherent to the predetermined *Unocal* standard, its actions will not be invalidated.

The reconnaissance provided undoubtedly shows Delaware's courts abstention to second-guess board's actions if adherent to the standards provided. However, the unprecedented context witnessed during the early stages of the pandemic and the unexpected non-adversarial positions held by proxy advisors – historically opposed to boards' deploying defensive measures – led experts to speculate whether courts would have upheld unconventional defensive tactics. To fathom how boards tried to thwart hostile bids and the outcome of the consequent litigation, it is necessary to investigate both the pandemic scenario and Delaware's decision in the seminal *Williams* case.

[159] WL 1922029 (Del. Ch. 2014).

[160] *Id.* at *46. The Court has found that "Plaintiffs have not shown a reasonable likelihood that they will be able to demonstrate that the Rights Plan is either coercive or preclusive".

[161] *Id.* at * 24-25. The board deployed the two-tier plan deeming acquiring persons "those who report their ownership in the Company pursuant to Schedule 13G up to a 20 % interest in Sotheby's". Instead, for those filing a 13D schedule, an acquisition of merely 10 % shares would have triggered the plan.

[162] *Ibidem.* The qualifying offer prescribed that the rights plan would not have triggered if the bid was for "any - and-all" shares of the company and if it gave the board at least 100 days to evaluate the offer.

[163] Quoting *In re Netsmart Techs., Inc. S'holders Litig.*, 924 A.2d 171, 191 (Del. Ch. 2007), the Court found that, in order to obtain a preliminary injunction, plaintiff had to show (i) a reasonable probability of success on the merits; (ii) that absent injunctive relief, they will suffer irreparable harm; and (iii) that the balance of the parties' harms weighs in favor of injunctive relief. It is a conjunctive test; therefore, all the elements must be proven.

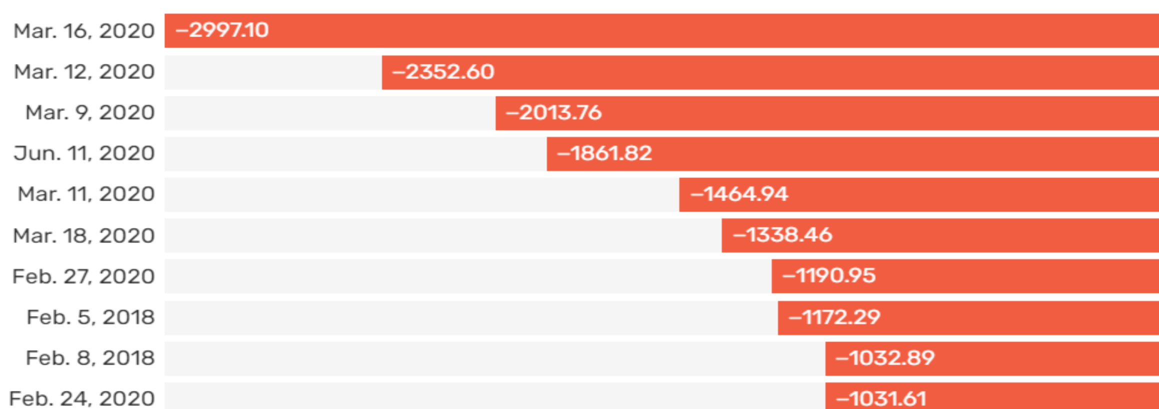
[164] *Thirdpoint* at *41. Quoting *Selectica* at 600, the Court found the presence of a majority of independent directors, advised by financial and legal counselors apt to demonstrate a *prima facie* showing of good faith and reasonable investigation.

[165] *Id.* at *47.

IV. THE *WILLIAMS* CASE AND THE END OF CRISIS PILLS

A. *Shareholder rights plan at the outbreak of the pandemic: a new pill?*

At the beginning of 2020, COVID-19 pandemic erupted and, as anticipated an unprecedented fall of market prices occurred. The graph below[166] vividly represents the atypical scenario as the market witnessed some of the worst economic collapses in history. The figure shows that the Dow Jones industrial average lost almost three thousand points in a single day, which represents a 12.9% loss[167].



In response to it, boards deployed pills of different kind both with conventional and unconventional trigger thresholds, and tailormade provisions. Consequently, given the extraordinary crisis – occurred due to the restrictions imposed on firms rather than exogenous shocks – a question rapidly saw the light of the day: "Should Boards be allowed to opt for unconventional defences? And if so, to what extent?". The unprecedented fall of the stock market in March 2020 in fact, reflected also on corporate governance as directors had to face a challenging decision which is how to prevent hostile bidders from acquiring control at bargain. Amongst the possible defensive tactics to oppose unsolicited bids, boards recurred to shareholders right plans (both traditional and NOL pills) which, as a result, peaked in March

[166] *See* the graph by Standard & Poors, *10 Biggest One-Day Point Losses in Dow Jones history* (2020), thebalance.com, https://www.thebalance.com/search?q=10+biggest+one-day+point+losses.
[167] *See* Lucy Bayly, *Dow slides 3,000 points in grisly day on Wall Street, despite massive intervention from Fed* (2020), CNBC.com, https://www.nbcnews.com/business/markets/dow-falls-2-200-points-trading-halted-rate-cut-fails-n1160246.

and April 2020, and approximately returned to their pre-pandemic level by the end of the same year. Specifically, 49 companies in just 2 months employed shareholder rights plans, while only 25 amongst the S&P 500 had them in place at the end of the previous year[168]. The worst hit industries were the entertainment, commodities and airlines; the plunge in the share prices rendered companies belonging to those sectors vulnerable to hostile takeover attempts. Clearly, it does not come as a surprise that those companies introduced unconventional defensive measures to fend off those attacks[169].

The situation described called for a firm board's intervention because companies were vulnerable to hostile bidders' takeover attempts and exposed to coercive offers. And poison pills are best suited for this task as they can be approved before the threat but adopted following to a coercive offer – the so-called "on the shelf" poison pills[170]. As a consequence of the extraordinary shock, commentators believed those threats could have justified at least the first prong of the *Unocal* standard in light of the company's vulnerability. As mentioned above, however, directors have also the burden to prove that the defence was reasonable to the threat perceived – the second prong of the *Unocal* test – therefore they shall be exceptionally prudent in choosing the right balance to protect the shareholder value while avoiding their entrenchment.

The main risk for the company is represented by a change in the control, which during the past COVID -19 crisis was fed by the suppressed share price which did not represent the company's fundamental value. Secondly, high-volume trades further threatened management because raiders could obtain control by exploiting the undervalued price and the shareholders' need for short-term liquidity. Finally, share prices drops affected firms' creditworthiness and credit institutions shrank credit thereby impairing companies' financial structure. Conversely, the main risk for stockholders was board entrenchment: directors could justify a preclusive defensive tactic with the need to protect shareholder value.

Although it is not unusual for boards to take advantage of market disruption to entrench itself, the need to protect the shareholder value led directors to adopt shareholder rights plans which, despite being considered as one of the most effective takeover defences, have been

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[168] See *Eldar & Wittry supra* note 18.

[169] As an example, Dave and Buster's (entertainment) and Williams co. (commodity). Their defences will be extensively treated later.

[170] *See* David Katz & Sabastian V. Niles*, Rights Plans ("Poison Pills") in the COVID-19 Environment "On the Shelf and Ready to Go"?* (2020), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2020/04/02/rights-plans-poison-pills-in-the-covid-19-environment-on-the-shelf-and-ready-to-go/ where they advocate for an easily deployable pill and suggest boards to have it "on the shelf and ready to go" to thwart hostile bids.

subject to a never-ending debate on the benefits and downsides enjoyed by corporations both in a long or short-term perspective. It is fair to say that, when adopting a shareholder rights plan, directors are mostly concerned with the subsequent boost it gives to the market value (short-term effect) rather than the negative consequences (in terms of long-term growth) to which the plan exposes the company.

Proxy advisors strongly effected the debate as they are overly cautious in analysing the defensive measures adopted by corporate boards; and commonly oppose those defensive mechanisms. Firms such as ISS and Glass Lewis[171] in fact, have frequently called into question the adoption of poison pills. Moreover, their recommendations clearly influence shareholder votes[172] and this has led to a widespread scepticism about the effectiveness of the pills. However, at the outbreak of the pandemic, something changed as proxy advisors started not to stand up against poison pills and considered the pandemic a right cause to deploy the shareholder rights plans. In their 2020 guidance, both ISS and Glass Lewis were very precise about the type of pill to prefer. The first recognised the share price drop as a valid justification for the adoption of a one-year pill. Further, it added it would have carefully reviewed the disclosed rationale for adopting the plan, the specific provisions embedded, and the trigger threshold – valuated holistically "within the context of the rationale provided and the length of the plan adopted, among other factors"[173]. For what concerns the shareholder approval, it encouraged boards to have the plan ratified by stockholders but reported a failure to do so in the short-term would not be fatal. The latter issued a similar guidance for the duration and rationale. It further added it would vote against the re-election of the board members renewing the rights plan without seeking for shareholder approval. Differently from ISS, it did not specify the threshold trigger level, but supported a 5 % poison pill.

This unexpected opening towards the pill could be interpreted as a mere temporary and fact-specific change of route or, following a speculative approach, as a less adverse opinion of the proxy advisors on shareholder rights plans, especially at time of crisis. Regardless of that, many companies deployed rights plans, both conventional and unconventional. The first were upheld, while the latter were enjoined. Again, courts confirmed the predetermined standards.

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[171] Two of the most important American proxy advisory firms.

[172] *See* James R. Copland et al., *The Big Thumb on the Scale: An Overview of the Proxy Advisory Industry* (2018), Stanford University Graduate School of Business Research Paper No. 18-27, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3188174 at *4 where they state that there is "considerable evidence that proxy advisory firms influence proxy voting outcomes".

[173] *See* Paul J. Shim et al., *ISS and Glass Lewis Guidances on Poison Pills during COVID-19 Pandemic* (2020), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2020/04/26/iss-and-glass-lewis-guidances-on-poison-pills-during-covid-19-pandemic/.

One of the first S&P 500 companies to adopt the defensive mechanism was Occidental Petroleum which, on 13 March 2020, announced the plan. It deployed a one-year pill, with a 15 % trigger level and subjected it to shareholder vote in the following general meeting in May[174]. The plan was clearly in line with the proxy advisors' directions and was adopted in response to the 60 % share price drop suffered by the company in March due to collapsing oil valuations. Subsequently, a notorious activist sought to replace the board by increasing his equity up until 9.9 % and harshly criticised the company's past M&A transaction – historically those critiques prelude a takeover attempt. These two events vividly testify a sensible threat to the company was present and the board had a duty to protect the shareholder value. It does not come as a surprise that given the perceived threat and the plan's compliance to the regular provision, the pill was not even litigated. The market also was in favour of the plan, and the day of the announcement, its stock price skyrocketed rising by 19.9 % on a daily basis.

Few days later, on 19 March, Dave and Buster's entertainment announced the adoption of a plan. The company had been seriously hit by the crisis and its market capitalisation had reduced to $237 million, down from $ 1.4 billion in January. The plan was similar to Occidental Petroleum's as they both proposed a one-year plan and did not expressly cite the pandemic as a cause for the defensive tactic[175]. However, its threshold was slightly different as it employed a two-tier trigger with a 15 % ownership level for 13D filers (*i.e.,* common shareholders) and a 20 % for 13G filers (*i.e.*, institutional investors). This company was subject to takeover attempts too as two private equity firms acquired 15 % shares overall in the two months prior to the adoption. Following to the plan, the market value sharply rose with a peak of 76.6 % on the announcement day.

Finally, Delek US Holdings, on 20 March 2020 announced a new plan. Operating in the commodities industry, it suffered from the reduction in oil demand. Again, its market capitalisation reduced by more than 100 % in two months. Its plan shared the trigger level (15 % with no exception for passive or institutional investors) and the duration with the previous two but stood out as it expressly cited the COVID-19 pandemic as a proximate cause for the adoption. In a release, the board precisely stated: "given the fact that Delek's current share price does not reflect the company's intrinsic long-term value due to the extreme dislocation caused by the COVID-19 crisis and low commodity prices, we have no choice but to take action

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[174] *See* Gail Weinstein et al., *A Turn Back to "Poison Pills" in Response to the Coronavirus Pandemic* (2020), HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2020/04/09/a-turn-back-to-poison-pills-in-response-to-the-coronavirus-pandemic/.

[175] *Ibidem.*

to prevent a creeping change of control without a premium on terms that would not deliver sufficient value for all shareholders"[176].

Departing from the examples provided, three considerations are to be made: one concerning the share price increase, a second about the effective characteristics of the pill and the final on the non-opposing position of the proxy advisors.

Concerning the market value, evidence shows how all companies enjoyed a share price increase, conversely from what happened to comparable firms. The effect in terms of shareholder value is evident as the new higher price deters hostile bidders by imposing an augmented economic burden to acquire control. Those activists should then readapt their takeover strategy but can still acquire control, yet at a higher cost. Critics usually argue the sharp rise is due to a mean-reversing effect as the company's value recovers from the fall or may only reflect the different pandemic stages. Still, the poison pill hinders bidders' acquisition plans. Then, what stems from the previous examples is also that boards were cautious in drafting the provisions and adapted the poison pill to the new scenario – as an example Occidental required shareholder' s approval to renew the plan and it is fair to say that poison pills became crisis pills. Finally, the non-opposing position of proxy advisors boosted the adoption of such pills as they have notoriously advised shareholders to abstain from or vote against directors when they deployed a defensive tactic that could potentially entrench the board.

Therefore, considering the proxy advisors unusual positions, the adapted version of poison pills and their proven effect on shareholder value, a question arose: "Should a litigation occur, were the standards previously consolidated by Delaware Courts suitable to curb abuses and speculations and protect legitimate behaviours?" In other words, "Will poison pills be judged in a more director-friendly manner, given the circumstances?". Nowadays these questions are not on sight anymore as the evergreen standard is still applied and was not modified nor revised during the pandemic. Judges, in fact, were irremovable in the application of the *Unocal* because markets rapidly recovered[177] from the crisis (with a sharp decrease in value and an even faster reaction) that also caused poison pills to be removed. However, market players and corporate agents could not anticipate how courts would have scrutinised

[176] *See* the release at https://ir.delekus.com/2020-03-20-Delek-US-Holdings-Adopts-Limited-Duration-Shareholder-Rights-Agreement.
[177] Chris Bradley & Peter Stumpner, *The impact of COVID-19 on capital markets, one year in* (2021), McKinsey & Company, https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/the-impact-of-covid-19-on-capital-markets-one-year-in.
In this article it is demonstrated how by the end of 2020 the market fully recovered its loss surpassing its maximum pre-covid crisis level of 19 February.

unconventional plans. The decision in the *Williams* case clarified any potential doubt and shed the light on the suitability of the standard to rule over the subject. To analyse how Delaware courts have decided upon an unconventional poison pill and examine the approach it followed at trial, it is necessary to delve into *The Williams Cos. Stockholder Litigation*[178].

B. Williams *and crisis pills*

1. The Plan's characteristics

Williams is a publicly traded energy company with its headquarters in Tulsa, Oklahoma. It owns and operates natural gas infrastructure assets, handling around 30 % of U.S. natural gas volumes. In the months preceding COVID-19, Williams enjoyed a relatively stable stock price, reaching a high of $24.04. After the U.S. declared a public health emergency due to COVID - 19, however, its stock price fell to $18.90 by the end of February 2020; therefore it deployed a one-year plan. As aforementioned, poison pills were originally conceived as anti-takeover devices, later they were redirected to address other corporate purposes such as protecting net operating loss assets, and only recently they have been deployed to defend against stockholder activism. The Williams board, in particular, identified three causes for the adoption of the plan: the desire to prevent stockholder activism during a time of market uncertainty and deflated stock prices – although the board was not aware of any specific activist plays afoot; second, the apprehension that hypothetical activists might pursue "short-term" agendas and contrast board's long-term strategy; and third, the concern that activists might stealthily and rapidly accumulate Williams stocks and win control. The shareholder rights plan adopted was unprecedented as it contained an extreme mix of features Delaware Court of Chancery has never evaluated before: a 5 % trigger threshold, a broad definition of "acquiring person" capturing beneficial ownership as well as ownership of derivative interests such as warrants and options, an expansive definition of "acting in concert, and a narrow definition of "passive investor"[179].

The Plan had a duration of 1 year and, when triggered, the rights were distributed on "the close of business on the tenth Business Day after a Person (defined as an individual, firm, or entity) acquires beneficial ownership of 5 % or more of Williams stock or commences a tender

[178] *The Williams Companies Stockholder Litigation*, Consol. C.A. No. 2020-0707-KSJM (Del. Ch. 2021).
[179] *Id.* at * 21.

or exchange offer that would result in their ownership reaching that threshold"[180]. Given Williams' market capitalization in March 2020, triggering the 5 % threshold at the time the Plan was adopted would have required an economic investment (sometimes referred to as a "toehold") of approximately $ 650 million[181]. In drafting the beneficial ownership definition, the board revisited Rule 13d–3 of the Exchange Act to include "certain synthetic interests in securities created by derivative positions" such as warrants and options. By doing so, it went beyond the rule[182] which already provided an equitable defence against takeover attempts; as a result, many stockholders were deemed beneficial owners.

Turning to the third element, the AIC Provision deemed a Person to be acting in concert with another, where the person knowingly acted in concert or in parallel towards a common goal (related to changing or influencing the control of the company) with another or was in connection with or as a participant in any transaction having that purpose or effect. Another requirement was for each person to be conscious of the other person's conduct and the presence of at least one additional factor to be determined by the board – exchanging info, attending meetings, conducting discussions, or making or soliciting invitations to act in concert or in parallel were typical additional factors to be evaluated by the board[183]. At first glance, it may seem a reasonable provision, but the additional factor gives directors a great leverage to determine whether two or more shareholders were deemed to act in concert. For this reason, the "parallel-conduct" dimension of the "acting in concert" clause is sometimes referred to as a "wolfpack" provision[184]. This feature long has been included in shareholder rights plans, but early poison pills required express agreements, using language that tracked the definitions of a "group," "affiliate," and "associate" under Section 13(d) and Rule 12b-2 of the Exchange Act.[185] The wolfpack provision adopted by the Williams' board, instead, did not "require an express agreement between two parties in order for the Board to conclude they were "acting in concert" for purposes of calculating the pill's ownership trigger. This demonstrates how the provisions exceeded federal law boundaries.

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[180] *Id.* at * 22.
[181] *Id.* at * 23.
[182] Following the filing of an initial Schedule 13D, the SEC requires an activist to file an amendment within one or two business days after each additional one percent acquisition of securities. For a company with an existing activist, this amendment might be a good early-warning indicator of when to activate a rights plan. *See* Elizabeth Ising, *Reconsidering Poison Pills* (2020), Gibson Dunn, https://securitiesregulationmonitor.com/Lists/Posts/Post.aspx?ID=39.
[183] *See Williams* at * 23.
[184] *See supra* note 81.
[185] See Caley Petrucci & Guhan Subramanian, Pills in a World of Activism and ESG, U. Chi. L. Rev. (forthcoming 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4104799.

Furthermore, the AIC Provision included a daisy chain concept, providing that "a person who is Acting in Concert with another Person shall be deemed to be Acting in Concert with any third party who is also Acting in Concert with such other Person"[186]. Put differently, stockholders are deemed to act in concert with one another by separately and independently acting in concert with the same third party. The provision was even more stringent because, although it allowed stockholders to initiate a proxy contest and solicit proxies without triggering the plan, it did not exempt routine communications among stockholders before the launch of a proxy contest or tender offer. Therefore, in principle, all shareholders, exchanging info despite not participating in the proxy battle, could be deemed to act in concert. Finally, the AIC Provision was also asymmetrical. It excluded "actions by an officer or director of the Company acting in such capacities," such that incumbents can act in concert without suffering the consequences of the Plan.[187]

The Plan's fourth characteristic was the exemption of passive investors from the definition of acquiring persons[188] to ensure that those shareholders would not be deemed to be a threat for the company under the plan. Director defendants testified as to their belief that the definition excludes Schedule 13G filers, defined under the Exchange Act[189] as investors that "acquired such securities in the ordinary course of business and not with the purpose nor with the effect of changing or influencing the control of the issuer".[190] Breaking down the clause, the exemption was quite hard to achieve because the requirements were conjunctive – *i.e.,* an investor had to meet all of them in order to grant the status of passive investor. However, even

[186] *See Williams* at *25.
[187] *Ibidem.*
[188] *Id.* at *26-27. The Plan defined "Passive Investor" to mean: [A] Person who (i) is the Beneficial Owner of Common Shares of the Company and either (a) has a Schedule 13G on file with the Securities and Exchange Commission pursuant to the requirements of Rule 13d-1(b) or (c) under the Exchange Act with respect to such holdings (and does not subsequently convert such filing to a Schedule 13D) or (b) has a Schedule 13D on file with the Securities and Exchange Commission and either has stated in its filing that it has no plan or proposal that relates to or would result in any of the actions or events set forth in Item 4 of Schedule 13D or otherwise has no intent to seek control of the Company or has certified to the Company that it has no such plan, proposal or intent (other than by voting the shares of the Common Shares of the Company over which such Person has voting power), (ii) acquires Beneficial Ownership of Common Shares of the Company pursuant to trading activities undertaken in the ordinary course of such Person's business and not with the purpose nor the effect, either alone or in concert with any Person, of exercising the power to direct or cause the direction of the management and policies of the Company or of otherwise changing or influencing the control of the Company, nor in connection with or as a participant in any transaction having such purpose or effect, including any transaction subject to Rule 13d-3(b) of the Exchange Act, and (iii) in the case of clause (i)(b) only, does not amend either its Schedule 13D on file or its certification to the Company in a manner inconsistent with its representation that it has no plan or proposal that relates to or would result in any of the actions or events set forth in Item 4 of Schedule 13D or otherwise has no intent to seek control of the Company (other than by voting the Common Shares of the Company over which such Person has voting power).
[189] 17 C.F.R. § 240.13d-1(b)(1)(i).
[190] *See Williams* at *27.

a disjunctive reading of the provision would have resulted in a narrow exemption. In fact, at the time the board adopted the plan, it had only three 13G filers (the necessary condition to be exempted); consequently, it all boiled down to excluding BlackRock, Vanguard, and State Street from the definition of acquiring person. A quite narrow exemption considered that these investment companies do not engage in hostile bids by default.

The board scheduled the first meeting to adopt the plan on 18 March and, despite it had not received a copy of the poison pill, decided to deploy it. Therefore, the following day, it started preparing the proxy statement for the general meeting to be held the next month, but directors did not disclose neither they were considering the plan nor that the renewal of the plan was not to be subject to a shareholder vote, conversely from other crisis plans[191]. Consequently, the market and the largest shareholders reacted negatively to the plan. ISS also challenged the plan on three levels: the 5 % threshold, the lack of a perceived threat and the failure to consider alternative defensive measures. Firstly, it believed the threshold level was not in line with comparable plans and it could damage shareholders as the market recovered; secondly it noted the board failed to address contingent threats resulting in a change of control; thirdly it stated the board seemed not to consider its recommendations to deploy a less stringent pill, with a higher threshold and a shorter term[192]. In addition, ISS suggested it would have recommended to vote against a director in the following election. Despite those concerns, the board which had the authority to redeem or amend the plan, opted not to do so.

Consequently, a lead shareholder filed litigation on 27 August.

2. The case

Plaintiff Steven Wolosky filed litigation on 27 August and was followed by plaintiff City of St. Clair Shores Police and Fire Retirement System with a similar action on 3 September. The court granted expedition on 8 September and consolidated the two actions on 15 September. They complained a direct claim for breach of fiduciary duty against director defendants seeking declaratory and injunctive relief regarding the validity and enforceability of the plan.

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[191] As previously anticipated, Occidental petroleum, which operates in the same industry and suffered from the oil price decline, subjected the renewal upon shareholder's vote.

[192] The concerns on the duration posited on the assumption stock prices would have recovered soon. This eventually happened as in less than three months, in June, the market value of the Williams company had reached its pre-pandemic level. *See supra* note 178 at *34. In fact, the crisis seemed to have caused a sharp price decline, followed by an even steeper rise, thereby defining a V-shape path, rather than a U-shape path (with a decline and a long and slow recovery).

The Chancery Court first asserted the nature of the claim: direct or derivative. Plaintiffs argued it was direct while defendants sustained it was derivative and thus subject to Court of Chancery Rule 23.1[193], which requires plaintiffs to either make a pre-suit demand on the board or to demonstrate that demand would have been futile. In 2004, the Delaware Supreme Court established a two-part test for determining whether claims are direct or derivative in *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*[194], a two-prong standard inquiring on (i) who suffered the alleged harm (the corporation or the suing stockholders, individually), and (ii) on who would receive the benefit of any recovery or other remedy (the corporation or the stockholders, individually). Since then, all poison pills cases had been addressed as direct. The defendants, instead, sought to apply the "special injury test"[195] to address its nature and relied on the *Moran* "derivative presumption"[196]. The Chancery Court rejected this second claim and applied the *Tooley* standard. The Vice Chancellor's choice seemed reasonable as improper poison pills work an injury on stockholders directly by interfering with at least three of the fundamental stockholder rights: the rights to vote, sell and sue.[197] Moreover, subsidiary rights depart from those – including the right to communicate with other stockholders,[198] nominate directors,[199] and communicate with (and even oppose) management and the board[200] – which directors altered through the proposed poison pill. Ergo, this articulation of the harm affected equity holders directly, and enjoining the pill was a remedy affecting stockholders alone, not the company.

Secondly, the Court ruled over the dispute on the applicable standard of review. On one side, claimants believed the *Unocal* was suitable for the case, on the other side defendants proposed a more deferential business judgement standard. The latter timidly stated *Unocal* was not the proper standard because the enhanced judicial scrutiny is justified only when "the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders"[201]. The Court rejected defendants' attempt to minimise

[193] Defendants argued that plaintiffs did not make a pre-suit demand and have failed to demonstrate demand futility. Therefore, they required judgement to rule their favour. *Id.* at 36.
[194] 845 A.2d 1031, 1033 (Del. 2004).
[195] The special injury test was first applied in *Moran* by the Chancery Court. *See supra* note 116.
[196] In *Moran* the Chancery court stated: "where, as here, no shareholder is presently engaged in a proxy battle, and the alleged manipulation of corporate machinery does not directly prohibit proxy contests, such an action must be brought derivatively on behalf of the corporation" *Id.* at 1070. Therefore, director defendants sustained the claim was derivative as no shareholder was engaged in a proxy battle.
[197] "Modern corporate law recognizes that stockholders have three fundamental, substantive rights: to vote, to sell, and to sue." *Id.* at 1069–71.
[198] *B.F. Goodrich Co. v. Nw. Indus., Inc.*, 1969 WL 2932, at *2 (Del. Ch. 1969).
[199] *Harrah's Ent., Inc. v. JCC Hldg. Co.*, 802 A.2d 294, 310–11 (Del. Ch. 2002).
[200] *Abajian v. Kennedy*, 1992 WL 8794, at *6 (Del. Ch. Jan. 17, 1992).
[201] *See Unocal* at 954.

board's entrenchment risk and easily dismissed the claim by noting that in a subsequent decision, the Supreme Court stated that all poison pills have a potentially entrenchment effect.[202]

Consequently, the Court entered the analysis on the substantive merits of the decision, and investigated the reasonable threats individuated and the specific board's response. Namely, the plan barely satisfied the first prong of the analysis – the "reasonableness test" – but its characteristics were so aggressive that the Court had to enjoin it; therefore, it didn't pass the "proportionality test". The opinion seemed reasonable as the plan presented an excessively low threshold and broad provisions; in addition, the board approved it regardless shareholder's approval or ratification – differently from what proxy advisors recommended. The Vice Chancellor deemed the plan preclusive and in opposition to shareholder's interests and confirmed the applicability of the *Unocal* standard even in an emergency context.

For the foregoing reasons, V. C. McCormick stated that the pills exceeded what it was reasonable to expect and failed to comply with the second prong of the standard. Furthermore, the decision to discuss only approximately the elements of the plan was a clear breach of the duty to act in an informed way, which should be the first concern of a thoughtful director. Finally, judgment was entered in favour of the certified class declaring the plan unenforceable and permanently enjoining the continued operation of it. *Williams* was the perfect opportunity for the Chancery Court to consolidate the established standards. Indeed, despite the adoption of defensive tactics was in line with the trend historically occurred in times of crisis following to a drop in share value, despite the proxy advisors' non-opposition had cleared the way for the pressures of the large law firms in favour of these operations, the indiscriminate adoption of poison pills did not pass the scrutiny of jurisprudence.

3. Decision and direct implications

What stems is that, despite it is not unreasonable to contrast overly aggressive activists' campaigns, board's justification that "all stockholder efforts to change or influence corporate direction constitute a threat to the corporation"[203] runs directly contrary to the ideological underpinnings of Delaware law. Again, whilst a poison pill may in principle deter raiders' lightning strike attacks, the defence shall still be proportional to the threat posed.

[202] *See Selectica* at 599.
[203] See *Williams* at * 65.

Having individuated the nature of the claim – direct – and the standard to apply – *Unocal* –, the Vice Chancellor then inquired board's intent in deploying the plan. The reasoning already raised some criticism as the "lawyer-drafted documents to which one would typically look for a statement of a board's purpose – *e.g.,* board resolutions, board minutes, company disclosures – do not reflect the Board's actual intent"[204]. In fact, while the board's meeting materials, press release and proxy supplement specify the plan was drafted "as a takeover deterrent"[205], the Plan was not adopted to protect against any specific threat at all as the board was not acting to "preserve any specific asset like an NOL. Instead, the Board was acting pre-emptively to interdict hypothetical future threats"[206]. Having said that, the Court was not concerned about the process taken by the board, and the good faith reasonable investigation seemed confirmed. Rather, it inquired into the threats individuated and the reasonableness of the response.

Turning to the first prong, the Court identified three possible threats the board might have considered in order to put in place the plan: (i) the desire to "prevent stockholder activism during a time of market uncertainty"[207], (ii) the desire to insulate the board from activist investors that might pursue "short-term agendas or distract management"[208] and (iii) the "concern that activists might swiftly accumulate over 5 % of the shares"[209]. Addressing the first question, the Court rejected the possible threat and concluded that under Delaware law, directors are not permitted to justify their actions by arguing that, without intervention of the Board, stockholders would "vote erroneously out of ignorance or mistaken belief"[210] in the election of directors[211]. In fact, directors' justification implied that all shareholders efforts to change or influence corporate direction constitute a threat. Clearly, this runs contrary to Delaware law. Then, it analysed the second alleged threat. Defendants argued there was a concern some investors would operate so to get immediate gains regardless the corporation's going concern. Neither this justification was accepted by the Court mainly for two reasons: again, this argument boils down to the we-know better approach and, whilst actual short-termism might be considered harmful for the company, hypothetical versions of it are not.

Finally, the last threat. The most controversial concerning the gap-filling role of the plan. It is referred to a tangible concern many scholars have underlined: the possibility to swiftly

[204] *Id.* at * 52.
[205] *Ibidem.*
[206] *Id.* at *53-54.
[207] *Id. at* * 63.
[208] *Ibidem.*
[209] *Ibidem.*
[210] *Id.* at * 65.
[211] This is known as the "we know better explanation".

accumulate a substantive number of stocks during the 10-day period before disclosure of acquisition of beneficial ownership[212]. In fact, there are particular concerns about the so-called lightning strike attacks which are rapid, undetected accumulations of stock in a short period of time. The Court's decision was very problematic because, if on one side it is reasonable to believe that activists can swiftly accumulate stocks in the ten-day window, upholding directors' justification would have meant boards can deploy shareholder rights plans whenever they wish. The Vice Chancellor upheld the justification but was careful in noting that the Court's task is not to determine whether a gap-filling purpose justifies the adoption of a plan, but rather to proceed with the analysis and determine whether the response was proportional to the perceived threat.

In analysing the effective reasonableness of the response, the Court sharply criticised the main features of the plan; therefore, it invalidated the pill. It first stated the 5 % threshold was unusual[213]; then it noted the plan's beneficial ownership definition went beyond the default federal definitions and captured also synthetic interests, such as options[214]. Subsequently, it reported the plan's passive investor definition exceeded the influence-control default of federal law to exclude persons seeking to direct corporate policies[215]. To conclude, the Court strongly opposed to the most critical aspect of the plan: the acting in concert provision. The board's provision in fact, with its broad language, swept up potentially benign stockholders communications "related to changing or influencing the control of the company"[216]. By doing so, even attending investor conferences or voting the same corporate action could have implied acting in concert. This limitation could potentially chill shareholder interaction upon which a sound governance depends. Moreover, the daisy chain provision operated to aggregate stockholders even if members of the group had no idea the other equity owners existed. To sum up the review, the Court even accepted the gap-filling role of the pills, but the measure didn't pass the second prong of the test: the proportionality of the response.

C. *Future developments of the pills*

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[212] Investors have a ten-day window to disclose their ownership when purchasing more than 5 % of outstanding shares. *See* Samir H. Doshi*, The Timing of Schedule 13D* (2020), HLS Forum on Corp. Gov.*,* https://corpgov.law.harvard.edu/2019/06/23/the-timing-of-schedule-13d/.

[213] *See Williams* at * 77. It is reported that only 2 % of all plans identified had a trigger lower than 10 %. In addition, even among those with such a low trigger, almost all were deployed in an NOL context.

[214] *Id.* at *78.

[215] *Ibidem.* at *78.

[216] Id. at *83.

Regardless of the decision in the *Williams* case, therefore, what emerges is simply that the safeguarding of the delicate balance between the protection of shareholders' interests and an opportunistic exploitation of target company's directors is to be ensured by the criteria developed before the pandemic crisis. A possible explanation for the Court's rigidity in the standard to apply is the quick rebound of the American economy and of the capital markets which avoided a drift towards standards of review that might have appeared more suitable to rule over the controversy between opposing shareholders and directors' interests. However, if on one side courts ruled out opportunistic adoptions of the plans, they also confirmed that a traditional version of the defensive tactic had some meritorious effects, or at least the damaging potential for shareholders was sufficiently constrained within an acceptable perimeter by the combination of a tight time horizon, shareholders' approval or ratification and a peculiar market situation. Further, it is also possible that the unconventional aggressiveness of the pill examined by the Court in the *Williams* case pushed judges towards a decisive censure; a moderate plan, examined at a more uncertain stage of the pandemic might have led to a different decision.

In the wake of *Williams*, one can only answer with certainty the question as to whether the *Unocal* standard also applies to defensive measures taken under emergency conditions. It can be concluded that the *Unocal* standard also disciplines those measures and that an overly aggressive pill does not meet the second part of the test. However, it cannot be excluded that the first prong, the reasonableness test, can be automatically fulfilled by the mere fact that a series of extraordinary circumstances coincide, as it was the case during the market crisis caused by the pandemic outbreak.

Certainly, given that the other plans were not subjected to a judgement, possibly because of their brevity or approval by the shareholders' meeting, a minimum indication might be inferred. One could deduce that, in circumstances of force majeure – that are in no way connected to company performance nor to the trend of an industrial sector or a portion of the market, but depend on elements that are completely extraneous, uncontrollable, and transversal to markets and territories, as the pandemic –, there is a generalised and tacit acceptance that a threat relevant in the framework of *Unocal*'s first prong is present. This thesis seems confirmed by the event that no shareholder has filed a litigation over the various crisis pills - except in *Williams*, of course. In fact, it is not absurd to imagine that the collapse of the stock markets was perceived as a threat to shareholder value and to the shareholders themselves, who were

worried about suffering an exploitation based on transiently hyper-depressed values for non-industrial reasons. Thus, on a purely speculative basis, eliminating the subjective – and overly aggressive – features of the instrument, it cannot be ruled out that the crisis pill could be, and perhaps have been, defensive mechanisms in which *Unocal*'s first prong could be taken for granted due to the pandemic emergency. This leaves open only the necessary proportionality test to be carried out on a case-by-case basis in relation to the technical prerogatives of the plans and the overall framework of the decisions taken by the board in the midst of the emergency scenario[217]. In fact, despite the Chancery Court expressly noted that the "board was not concerned about any specific activist threat"[218], nor was it protecting a particular asset, but had acted "to interdict hypothetical future threats"[219], it did not exclude in absolute terms the first prong of *Unocal*; as if to say, that, in principle, a crisis of this magnitude may be considered the opening valve to an indistinct series of future and possible, yet realistic, dangers which, once actualized, constitute the necessary threat. These speculations, however, remain entirely hypothetical and cannot be proven with certainty. Rather, they can be expressed as a more possibilistic opinion than would have been legitimately expected in non-emergency times. Again, it does not make much sense to project conclusions towards future similar scenarios, which probably - and hopefully - will not recur or will in any case do so with different connotations.

In view of the impediment caused on will-be stockholders, it is also possible to argue that shareholder rights plans' use may be extended to counter-push stockholder-centric positions, especially in this era of renewed shareholder activism[220]. The structuring of the pill is, in fact, also consistent with a policy to curb activism where it is aimed at gaining control. Especially in this new era of corporate governance, activism is gaining momentum as shareholders are exercising their vote power; then crisis pills can be employed by managers to thwart hedge funds and other highly engaged shareowners both in pre-bid – through public and private pressure in proxy contests – and post-bid scenarios. In this context, the change – albeit cautious and conditional – in the position of the proxy advisors in relation to the pill had certainly constituted an appreciable signal beyond the specific defensive tactics; when, however, the task

[217] *See* Pierluigi Matera & Ferruccio M. Sbarbaro, *Le Poison Pill dopo* Williams, 5 Il Nuovo Dir. Delle Soc. X (2022). They treat the matter extensively and insist on the Chancery Court's decision to consider the first prong satisfied despite acknowledging the board acted preemptively.
[218] *Id.* at *54.
[219] *Ibidem*.
[220] *See* Rich Thomas et al., *Q1 2022 Review of Shareholder Activism*, HLS Forum on Corp. Gov., https://corpgov.law.harvard.edu/2022/04/28/q1-2022-review-of-shareholder-activism/ where they show that in the U.S. in the first quarter of 2022 shareholder activism recorded a new high since 2018.

of verifying the general perimeter of the legitimacy of the defences fell to the jurisprudence once again – with *Williams* – it was made clear that the pandemic could not – and cannot – free the board from its duties in the context of anti-raider or even only anti-activist conduct. Therefore, shareholder rights plans remain a viable option to respond to potential changes of control, and it is not unreasonable to believe that the ever-green *Unocal* standard, despite its modifications and adjustments, will continue to be used to rule the subject. Consequently, poison pills' applications can be extended to a wide variety of cases and, in order to protect companies when the price is depressed – either due to an intrinsic firm-related issue or an external industry or market-related problem –, boards need to individuate a reasonable threat and deploy a proportional defensive mechanism in order not to incur liability.

V. CONCLUSION

At the beginning of 2020, a long dated defensive tactic returned to vogue as boards sought to defend corporations from hostile bidders. The trend outlined describes a vigorous deployment of poison pills in March and April 2020 and a gradual adjustment to pre-pandemic levels later during the year. As the unprecedented crisis impaired companies' assets, it was unclear whether courts would have applied a more lenient standard of review to scrutinise boards' decisions or if they would have sticked to their legal precedents; consequently, companies either employed conventional or atypical shareholder rights plans. The subsequent *Williams* decision confirmed the firmly established *Unocal* standard and closed the door to unconventional pills.

In view of all this, I argue that poison pills convey substantial benefits to companies, and the approval of a plan boils down to a reasonable response to a perceived threat.

In fact, as proven throughout 40 years of applicability, Martin Lipton's ingenious idea has empowered directors with an unrivalled defensive tactic which inevitably boosts share price, increases target board's bargaining power, reserves the company some time to carefully evaluate the proposals, and eventually slows down the acquisition process.

Firstly, despite commentators may believe soaring prices represent only a mean-reverting effect as companies gradually recover from the downfall, I contend poison pills adopters witness abnormally high returns with respect to comparable firms in the days following to the announcement. Besides, even a temporary rise in the share price will still work a deterrent effect on hostile bidders. Secondly, another implication of poison pills is an augmented boards' bargaining power and, given that the organ is vested with the power to negotiate the best deal possible – in compliance with the *Revlon* requirement – both shareholders and directors benefit

from it. The formers may realise a higher premium than by negotiating on their own – dispersed ownership implies diverging shareholders' interests –, the latter can remain in charge to serve the shareholder value. To maximise it, however, boards need time which the defence grants. I am convinced corporate fiduciaries are best suited to run the enterprise; therefore, should a long-term project be unfairly undervalued by the market, directors shall be endowed with a proper mechanism to fend off attacks and continue along the chosen path. In many cases, a corporate turnover may result detrimental for the company and, if not shielded, managers will drift towards short-termism, leaving longer-term profitable opportunities unexploited. Thirdly, I sustain that it shall be directors' final decision to accept, reject, slow down, or even pause an acquisition mechanism as their role to oversee the company requires them to be well-informed before taking a decision. This is in line with a founding principle of capitalism: the separation of ownership and control.

Furthermore, the pill's applicability extends to a wide range of scenarios as the board may choose from a long set of provisions and deploy tailor made plans apt to defend the company. In fact, as acquisition attempts differ from one another, the bastion of corporate governance shall be modelled to resist to striking attacks. And a tactic with few mandatory requirements and many ad hoc clauses serves the purpose. Additionally, following to the new season of activism, it can be speculated a threat to company's long-term value is present and shareholder rights plans may even be deployed to thwart off activist investors, still in compliance with the predetermined standards. Again, the chameleonic nature of the pill has been proved and an easily deployable, vigorous and effective defence is what boards need to maximise shareholder value.

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