

BAILEY CAVALIERI LLC
ATTORNEYS AT LAW

One Columbus 10 West Broad Street, Suite 2100 Columbus, Ohio 43215-3422
telephone 614.221.3155 facsimile 614.221.0479
www.baileycavalieri.com

AN OVERVIEW OF OHIO'S TAKEOVER LAWS

Prepared by
Thomas E. Geyer
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Michael Miglets of the Ohio Division of Securities contributed to this outline.

The material in this outline is not intended to provide legal advice as to any of the subjects mentioned but is presented for general information only. Readers should consult knowledgeable legal counsel as to any legal questions they may have.

I. BACKGROUND: THE SOVEREIGNTY OF STATE CORPORATE LAW AND THE CONSTITUTIONALITY OF BLUE SKY LAW.

- A. In general, Ohio's authority to enact laws governing takeover transactions results from the sovereignty of state corporate law and the constitutionality of blue sky law.
- B. The United States Supreme Court's recognition of the sovereignty of state corporate law has been longstanding, explicit and specific:
1. Without ascribing to this body, which in its corporate capacity, is the mere creature of the act to which it owes its existence, all the qualities and disabilities annexed by the common law to ancient institutions of this sort, it may correctly be said to be precisely what the incorporating act has made it, to derive all its powers from that act, and to be capable of exerting its faculties only in the manner which that act authorizes. Head & Amory v. The Providence Insurance Company, 6 U.S. 127, 167 (1804).
 2. By the term "corporate franchise or business" ... we understand is meant ... the right or privilege given by the State to two or more persons of being a corporation, that is, of doing business in a corporate capacity ... The granting of such right or privilege rests entirely in the discretion of the state, and, of course, when granted, may be accompanied with such conditions as its legislature may judge most befitting to its interests and policy. Home Insurance Company v. New York, 134 U.S. 594, 599-600 (1890).
 3. [T]he corporation is a creature of the State. It is presumed to be incorporated for the benefit of the public. It receives certain privileges and franchises, and holds them subject to the laws of the State and the limitations of its charter. Its rights to act as a corporation are only preserved to it so long as it obeys the laws of its creation. Hale v. Henkel, 201 U.S. 43, 74-75 (1906).
 4. Corporations are creatures of state law, and investors commit their funds to corporate directors on the understanding that ... state law will govern the internal affairs of the corporation. Cort v. Ash, 422 U.S. 66, 84 (1975).
 5. It is thus an accepted part of the business landscape in this country for States to create corporations, to prescribe their powers, and to define the rights that are acquired by purchasing their shares. CTS Corp. v. Dynamics Corporation of America, 481 U.S. 69, 91 (1987).

- C. In Hall v. Geiger-Jones, 242 U.S. 539 (1917), the United States Supreme Court upheld the constitutionality of state securities law based on “the power of the state to prevent frauds and impositions.” *Id.* at 551.

II. OHIO CONTROL SHARE ACQUISITION ACT, R.C. 1701.831.

- A. *Purpose:* To ensure that: (i) information regarding a proposed acquisition is timely delivered to the target company; and (ii) those who hold shares in the target company before the proposed acquisition is announced have a sufficient opportunity to both consider the information and vote upon the proposal.

- B. *Operative Provision:* Unless an Ohio corporation has "opted out" of the Ohio Control Share Acquisition Act, any "control share acquisition" of an "issuing public corporation" shall be made only with the prior authorization of the shareholders of the "issuing public corporation" in accordance with the Ohio Control Share Acquisition Act. R.C. 1701.831(A).

- C. *Selected Definitions.*

1. "issuing public corporation": an Ohio corporation with 50 or more shareholders that has its principal place of business, its principal executive offices, assets having substantial value, or a substantial percentage of its assets within Ohio, and as to which no valid close corporation agreement exists. R.C. 1701.01(Y).
2. "control share acquisition": subject to certain enumerated exceptions, an acquisition that would cross the one-fifth, one-third or majority share ownership thresholds. R.C. 1701.01(Z). (A significant exception is for a merger or consolidation adopted, or a combination or majority share acquisition authorized, by vote of the shareholders of the issuing public corporation in compliance with the Ohio General Corporation Law, R.C. 1701.)
3. “interested shares:” *See* II.D.3.c. below.

- D. *Requirements.*

1. A potential acquiror must deliver to the issuing public corporation's principal executive offices an "acquiring person statement" that sets forth certain minimum information about the acquiror and the proposed acquisition. R.C. 1701.831(B).
2. Within ten days after receipt of an "acquiring person statement" conforming to law, the issuing public corporation's directors must call a special meeting of shareholders for the purpose of voting on the proposed acquisition (the "831 meeting"). R.C. 1701.831(C)(1). With two

exceptions, the 831 meeting must be held within fifty days after receipt of the "acquiring person statement." *Id.* The exceptions are:

- a. The potential acquiror agrees in writing to another date. *Id.*
- b. If the potential acquiror: changes the percentage of the class of shares being sought, the consideration offered, or the security dealer's soliciting fee; extends the expiration date of a tender offer for the shares being sought; or otherwise changes the terms of the proposed control share acquisition, then the directors of the issuing public corporation may reschedule the 831 meeting. If the proposed control share acquisition is to be made pursuant to a tender offer, then the meeting may be rescheduled to a date that is not later than the expiration date of the offer. If the proposed control share acquisition is to be made other than pursuant to a tender offer, the meeting may be rescheduled to a date that is not later than ten business days after notice of the change is first given to the shareholders. R.C. 1701.831(C)(2).

3. Special quorum and voting standards are applied at the 831 meeting. R.C. 1701.831(E).

- a. Quorum: At least a majority of the voting power of the issuing public corporation in the election of directors is represented at the 831 meeting in person or by proxy. R.C. 1701.831(E)(1).
- b. Voting: The proposed acquisition must be approved by *both*:
 - i. a majority of the voting power of the issuing public corporation in the election of directors represented at the meeting in person or by proxy; *and*
 - ii. a majority of the voting power of the issuing public corporation excluding the voting power of "interested shares" represented at the meeting in person or by proxy. R.C. 1701.831(E)(1).
- c. "interested shares": generally, shares of the issuing public corporation held by a person who acquires such shares for consideration in excess of \$250,000 during the period commencing on the date of the announcement of the proposed takeover and ending on the record date for the 831 meeting, and post-record date transfers by such persons if voting power is also transferred. R.C. 1701.01(CC).

E. *Constitutionality.*

1. The constitutionality of the Ohio Control Share Acquisition Act has been litigated to conclusion on several occasions. The current state of the law is that the statute is constitutional. The statute is neither preempted by the federal Williams Act, nor unduly burdensome on interstate commerce. United Dominion Industries Limited v. Commercial Intertech Corp., 943 F. Supp. 857 (S.D. Ohio 1996).
2. Ohio law expressly recognizes the use of presumptions and forms of proxy in the conduct of shareholder meetings. R.C. 1701.832(D).

III. OHIO CONTROL BID STATUTE, R.C. 1707.041.

A. Background.

1. *The Ohio Takeover Act.*

Federal regulation of tender offers began in 1968 with the enactment of the Williams Act. Ohio followed in 1969 with the Ohio Takeover Act, R.C. 1707.041. This Ohio law required an offeror to make a public announcement and a filing with the Ohio Division of Securities (the “Division”) at least twenty days prior to commencement of the tender offer. The Division then had ten days to determine if a hearing was necessary. The target company could request a hearing. The hearing had to be held within forty days of the filing and a final adjudication had to be issued within sixty days of the hearing.

2. *Federal Preemption.*

The Williams Act required that a tender offer be open only a minimum of twenty business days. This conflicted with the Ohio Takeover Act, and a number of other state takeover statutes that required a “pre-commencement” filing of twenty days or more. Indeed, in 1979, the District Court for the Southern District of Ohio held that the Ohio pre-commencement filing requirement was preempted. AMCA International Corp. vs. Krouse, 482 F.Supp. 929 (S.D. Ohio 1979). After that decision, the Division continued to apply the Ohio Takeover Act *sans* the twenty day pre-commencement filing requirement. Then, in 1982 the United States Supreme Court struck down the Illinois takeover law in Edgar v. Mite, 457 U.S. 624 (1982). Many practitioners and commentators believed that this sounded the “death knell” for state regulation of takeovers.

3. *Revitalization of State Law.*

The reports of the death of state takeover regulation were greatly exaggerated. In 1984, in Cardiff Acquisitions v. Hatch, 751 F.2d 906 (8th

Cir. 1984), the Eighth Circuit Court of Appeals upheld the Minnesota Corporate Take-Over Act. The Minnesota law represented a new breed of state regulation that mandated certain disclosures and required a filing with the Minnesota state securities commissioner, but limited the state's role to ensuring that full and fair disclosure was made. In other words, the state did not have the authority to judge the merits or fairness of the transaction, and the court found that the state disclosure requirements and state review process were not inconsistent with the Williams Act. In addition, in 1987 the United States Supreme Court limited its decision in Edgar v. Mite by upholding the Indiana control share acquisition act in CTS Corp. v. Dynamics Corp. of America, 481 U.S. 69 (1987). The Cardiff and CTS Corp. decisions paved the way for a new wave of state takeover laws that were not inconsistent with the Williams Act.

In 1990, the Ohio Takeover Act was amended to become the Ohio Control Bid Statute. The twenty day pre-commencement filing requirement was replaced with a contemporary filing requirement, and the statute was otherwise amended to follow the Minnesota law that had been upheld in Cardiff.

B. Overview.

1. *Purpose:* To ensure that tender offers made for companies with significant ties to Ohio include full disclosure of material information.
2. *Operative Provision:* No "control bid" for any securities of a "subject company" may be made pursuant to a "tender offer" until the offeror files with the Division certain specified information, and also provides certain specified information to the shareholders of the "subject company." R.C. 1707.041(A)(1).
3. *Definitions.*
 - a. "control bid": subject to certain exceptions, a purchase of shares that causes the purchaser to be directly or indirectly the beneficial owner of more than ten percent of any class of the issued and outstanding equity securities of the target company. R.C. 1707.01(V).
 - b. "subject company": an issuer that *both* has its principal place of business, principal executive office, or at least \$1,000,000 worth of assets in Ohio, *and* more than ten percent of its beneficial or record securities holders are Ohio residents, more than ten percent of its equity securities are owned beneficially or of record by Ohio residents, or more than one thousand of its beneficial or record security holders are Ohio residents.

Note: This definition means that the Ohio Control Bid Statute has a broader applicability than the federal Williams Act. While the Williams Act is limited to "reporting companies," the definition of "subject company" includes both reporting companies and non-reporting companies.

- c. "tender offer": not defined in state or federal statutes or regulations; consequently, judicial tests have developed, e.g. Wellman v. Dickinson, 475 F. Supp. 783 (S.D.N.Y. 1979):
 - i. active and widespread solicitation of public shareholders;
 - ii. solicitation made for substantial percentage of target's stock;
 - iii. made at premium over prevailing price;
 - iv. terms of offer are firm, not negotiable;
 - v. offer contingent on tender of fixed number of shares;
 - vi. offer open only for a limited time;
 - vii. offeree subjected to pressure to sell;
 - viii. public announcements precede or accompany rapid accumulation.

Note: Not all factors need be present.

4. *Requirements.*

- a. A Form 041 and certain information must be filed with the Division:
 - i. all materials by means of which the offeror proposes to disclose the material terms of the transaction (R.C. 1707.041(A)(2)(a));
 - ii. the identity and background of the offeror (R.C. 1707.041(A)(2)(b));
 - iii. the source and amount of funds (R.C. 1707.041(A)(2)(c));
 - iv. a statement of any plans regarding liquidation, plant closings, lay-offs, amendment of benefit plans, or other major corporate changes (R.C. 1707.041(A)(2)(d));

- v. the number of shares held by the offeror (R.C. 1707.041(A)(2)(e));
 - vi. particulars as to any contracts or arrangements to which the offeror is a party with respect to any equity security of the subject company (R.C. 1707.041(A)(2)(f));
 - vii. detailed information about the corporate structure, operations and management of the offeror (R.C. 1707.041(A)(2)(g)); and
 - viii. such other information as is required to make full, fair, and effective disclosure of all material information (R.C. 1707.041(A)(2)(h)).
- b. The foregoing information and all material terms of the offer must be provided to the shareholders of the subject company. R.C. 1707.041(A)(1).
5. *Constitutionality:* The constitutionality of the Ohio Control Bid Statute has not been litigated to conclusion, but its constitutionality appears to have been enhanced by the 1990 amendments to the statute which eliminated conflicts with the federal Williams Act.
6. *Authority of the Division:* Within five calendar days of the date of the control bid filing, the Division may suspend the continuation of the control bid if the Division determines that all of the information required has not been filed with the Division or that the control bid materials do not provide full disclosure of all material information concerning the control bid. R.C. 1707.041(A)(3). If the bid is suspended, the offeror may request an administrative hearing before the Division, which must be held within ten calendar days of the date the suspension is imposed. The determination of the Division must be issued within three calendar days of the date of the hearing.

IV. OHIO BUSINESS COMBINATION STATUTE, R.C. 1704.

- A. *Purpose:* To prevent some of the abusive and self-dealing activities that often accompany or follow highly-leveraged acquisitions, and to encourage persons proposing an acquisition to negotiate with the board of directors of the target company so that all of the target's shareholders receive full and fair consideration for their shares.
- B. *Operative Provision:* Unless an Ohio corporation has "opted out" of the Ohio Business Combination Statute, the statute: (i) prohibits, for a period of three years, the consummation of "Chapter 1704 transactions" between the acquiror and an "issuing public corporation" unless the "issuing public corporation's" directors

have approved the acquisition or the proposed "Chapter 1704 transaction;" and (ii) limits the consummation of "Chapter 1704 transactions" after the three year moratorium unless the acquisition was approved by the "issuing public corporation's" directors, the "Chapter 1704 transaction" is approved by a specified majority of the "issuing public corporation's" shareholders, or the "Chapter 1704 transaction" meets certain statutory criteria designed to ensure that the "issuing public corporation's" shareholders receive consideration which is fair both in form and amount.

Note: One commentator has suggested that "the very complexity which makes compliance with the statute's limitations a forbidding challenge creates part of the incentive to avoid its bite." Friedman, *Ohio Securities Law and Practice* 745 (2nd ed. 1996).

C. *Definitions.*

1. "issuing public corporation": an Ohio corporation with 50 or more shareholders that has its principal place of business, its principal executive offices, assets having substantial value, or a substantial percentage of its assets within Ohio, and as to which no valid close corporation agreement exist. R.C. 1701.01(Y).
2. "Chapter 1707 transaction:" an extensive listing of transactions including: mergers, asset acquisitions, or exchange offers; distribution or transfer of substantial assets; distributions of stock or rights; liquidations; disproportionate recapitalization or similar transactions; and disproportionate receipt of valuable benefits. R.C. 1704.01(B).

D. *Requirements.*

1. The three year moratorium can be avoided if the "issuing public corporation's" directors approve: (i) the original acquisition; or (ii) the proposed "Chapter 1704 transaction." R.C. 1704.02.
2. Even after the three year moratorium, a "Chapter 1704 transaction" may be consummated *only* if: (i) the transaction is approved by both a two-thirds vote of all shareholders and a majority of "disinterested" shareholders; or (ii) a statutorily computed "fair price" is provided to minority shareholders.

E. *Constitutionality:* The constitutionality of the Ohio Business Combination Statute has not been litigated to conclusion, but the statute is based on the Wisconsin statute upheld in Amanda Acquisition Corporation v. Universal Foods Corporation, 877 F. 2d 496 (7th Cir. 1989).