The Conference Board Issues Poison Pill Recommendations

By Gary Larkin
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The recent Delaware Court of Chancery Air Products v. Airgas decision and the spate of poison pill adoptions in recent months lends credence to the theory that the anti-takeover shareholder rights plans are alive and well.

A Director Notes report entitled Poison Pills in 2011 released by The Conference Board Governance Center yesterday addresses the issue of poison pills and offers some recommendations for corporate boards to avoid becoming a hostile takeover target. The report, co-authored by Andrew L. Bab (a partner) and Sean P. Neenan (an associate) of Debevoise & Plimpton, states that while the shareholder rights agreement is no longer prevalent, recent case law shows that properly structured poison pills can be valuable anti-takeover devices.

Among the four recommendations in the report [Read March 17 press release], Bab and Neenan write that boards should:

- Consider drafting shareholder rights plans so that they satisfy standards of acceptability set by the most influential proxy voting advisors such as ISS while also taking into account such issues as derivative voting positions and net operating losses (NOL), which can be a valuable corporate asset until there is an ownership change.
- Consider having management maintain a thoughtful business plan for the corporation that the board understands and has approved.
- Consider abstaining from certain defensive tactics, such as introducing supermajority voting requirements or disallowing action by written consent or limiting the ability to call special meetings.
- Consider adopting advance notice bylaws so that directors can avail themselves of enough time to obtain the information necessary to make a rational business decision about the acquisition or merger offer.

“It will be interesting to watch for changes in poison pill activity taking place this proxy season, as companies react to the most recent developments in case law, hedge funds get back into the activism game, and M&A activity continues to grow,” Bab said.

By no means is the latest Director Notes report the only recent research on poison pills. According to an article on CFO.com (Poison Pills Haven’t Lost Their Potency), research from FactSet Research Systems shows that eight of 11 poison pills implemented in the first quarter of 2011 were adopted in response to an activist investor acquisition or to preserve the NOL carryforwards.

The article goes on to say that shareholder rights plans are being used more now as short-term stopgaps against impending takeover threats opposed to being insurance policies against corporate raiders.
And just last week, Family Dollar Stores began fighting off a hostile takeover by rejecting a multi-billion bid by a hedge fund and adopting a poison pill.

However, in a Feb. 24 Wall Street Journal Op-Ed piece (An Antidote for the Corporate Poison Pill) the well-known Harvard Law School professor and director of its corporate governance program, Lucian Bebchuk, warns that while the Delaware court decision upholds the validity of certain poison pills, pressure by shareholders could “substantially limit their toxicity.”

“That would produce considerable benefits for investors and for our capital markets,” Bebchuk wrote. He further explained Chancellor William Chandler’s logic behind his decision:

“Chancellor Chandler stated that he would have preferred to let shareholders make the choice at this stage, as they ‘know what they need to know . . . to make an informed decision.’ But he felt that denying shareholders’ right to choose was required by previous Delaware cases, which recognized directors’ right to block offers out of concern that shareholders would accept them ‘in ignorance or a mistaken belief’ concerning the value of remaining independent.”

Meanwhile, The Conference Board Governance Center will continue to provide guidance to public companies facing activist shareholders through its Director Notes series and the Shareholder Activism Report and Resource Portal, which was launched in April 2010 in collaboration with the following professional leaders in the field: Debevoise & Plimpton LLP; Egon Zehnder International; Georgeson Inc.; Hedge Fund Solutions, LLC; Innisfree M&A Incorporated; Joele Frank, Wilkinson Brimmer Katcher; MacKenzie Partners, Inc.; Sard Verbinnen & Co; Sullivan & Cromwell LLP; and Wachtell, Lipton, Rosen & Katz.