

Did Bill Ackman just kill the poison pill?

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The Valeant-Allergan fight shows that hedge fund activists are getting better at swallowing corporations' hostile merger defenses.

You might be able to add the so-called poison pill to the list of Bill Ackman's conquests this year.

On Tuesday, a judge in California ruled that Ackman is allowed to vote his shares at a key meeting next month in the long-running takeover battle for botox maker Allergan. Ackman favors a bid by rival pharmaceuticals company Valeant, which Ackman has teamed up with to acquire Allergan. Poison pills are supposed to stop investors from doing this sort of thing (i.e. ganging up with other investors or with other companies to do hostile take overs). Allergan has a poison pill in place, and has been fighting to stave off Valeant's takeover bid. And the judge's ruling means that Ackman and Valeant can continue to team up. It also means that Ackman, who will vote to have most of Allergan's board removed, and Valeant are one step closer to taking over Allergan.

Allergan may still thwart this effort. The company is reportedly [in talks](#) to be acquired by another pharmaceutical company, Activas.

Still, the ruling seems like a pretty big victory, not just for Ackman and Valeant, but for all activist hedge funds and would-be hostile acquirers.

Poison pills have been a thorn in the side of activist investors and acquisitive companies for nearly three decades. The provisions, established in the mid-1980s, were meant to stop corporate raiders, that decade's biggest threat. The classic corporate raider move was to find a company whose shares had plummeted and then offer to buy out shareholders at a higher price than what the company's stock was currently trading, but still maybe less than it would ultimately be worth. Still, shareholders looking for a quick buck would hand over their shares.

Poison pills made that move close to impossible. The provisions allow companies to offer cheap or free shares to shareholders who are friendly to the company and its current management. If a raider shows up, management floods the market with new shares to only those who are on their side. The raiders, however, who don't get the new shares, end up with a much lower stake in the company and shares that are worth much less than before. They could then try to buy up the new shares, but management could always just flood the market again. It's toxic to anyone trying to do this, which is where the name poison pill comes from.

But by teaming up to overthrow the board, rather than making a bid to shareholders, Ackman and Valeant may have come up with the ultimate antidote to the poison pill. Some don't want to admit that. Hours after the judge's verdict, prominent M&A law firm Wachtell Lipton Rosen &

Katz put out a memo claiming that the judge's ruling was actually a victory for Allergan and companies in a similar position.

Marty Lipton, a legendary corporate lawyer and the long-time head of Wachtell, has a lot at stake here. Not only is Wachtell on Allergan's legal team, but the poison pill is very much part of Lipton's legacy. Lipton is credited with inventing poison pill agreements back in the 1980s. Ackman and Lipton also personally don't have a lot of love for one another. Ackman settled a long-running dispute with Carl Icahn when they both agreed that they dislike Marty Lipton more than they dislike each other.

But even Lipton seems to think the poison pill isn't the defense it used to be, particularly in the age of activist investors looking to overthrow boards. The day after the ruling, Wachtell released another client memo, this time a three-page list of all the steps companies need to take to ward off an attack from an activist. "Reinforce your poison pill" wasn't one of them.

Of course, some of this is Lipton taking advantage of the situation. The win for Ackman is a pretty good time for Lipton to remind clients why you need Wachtell. Others don't think the poison pill has been totally bottled up. First of all, the judge's decision wasn't really about Allergan's poison pill provision. Allergan had actually given up on its poison pill as a defense a few months ago. But, presumably, it did so because it thought it would win on insider trading charges, which it didn't.

But Allergan didn't totally lose, either. The judge's ruling, which allows Ackman to vote his shares with Valeant, did say that there was something "insider trade-y" about the way that Valeant told Ackman about its plan to make a bid for Allergan before others. But the judge said that was for others to decide, though the judge made Ackman and Valeant disclose that their bid could have some legal risks. While that's not much of a win for Allergan—it wanted the judge to block Ackman from voting—it could cause some other hedge funds to pause from before following Ackman's lead, particularly at time when prosecutors have been aggressive about going after hedge funds for insider trading.

"I think this ruling will put a substantial chill on activist-corporate team ups," says John Coffee, a law professor at Columbia University. "The decision contained a sharp rebuke of Ackman's tactics. My guess is Lipton is very happy they got that."

What's more, the judge making the ruling was in the 9th circuit court in California, which is not where key rulings in M&A cases get made, and therefore holds a little less sway when it comes to setting precedent. That's usually the job of the 2nd Circuit Court of Appeals in New York for federal cases, or the Delaware court system, because that's where many companies are incorporated, for state cases. Allergan has said it is going to appeal the ruling.

Lucian Bebchuk, a Harvard professor who has called laws that uphold poison pills provisions unconstitutional in the past, isn't claiming a victory yet. He says the California judge's ruling doesn't change much. Activists always had the ability to vote out board members to get around poison pill agreements. "The poison pill remains highly relevant and [is still] the key defense tool that targets use to block offers," says Bebchuk.

So, what happens now? Here's the best guess: Allergan will hold its special board meeting in December. Most observers think that Valeant, with the help of Ackman's shares, now has enough votes to oust six of Allergan's nine board members. The rub is that Allergan's bylaws say that while shareholders can vote out board members, they can't appoint new ones. That job would go to Allergan's remaining board members. Those board members are likely to put in place new board members who are friendly to Allergan's current management.

At that point, Ackman would likely sue Allergan in Delaware court claiming that Allergan's board is not acting in the best interest of its shareholders. Columbia's Coffee says if Ackman wins that suit, with the court ruling that corporate boards have to defer to what shareholders perceive is in their best interests and not bylaws, then poison pills could finally be done.

"That would dramatically shift the power in takeover battles to hedge funds and activists," says Coffee.

The fact that the poison pill is less potent than it used to be is a sign that the balance of power is shifting already.