

DELAWARE POISON PILLS

The heightened global attention to corporate governance in the past 10 years has only been accelerated by the intervening financial crisis. In what some call “the biggest M&A case in 20 years,”¹ the Delaware Chancery Court recently considered who should decide the fate of a company: the board or the majority of the shareholders. With more than 850,000 business entities calling Delaware their legal home, including over 50% of all U.S. publicly traded companies and 63% of the Fortune 500, this decision is bound to have a significant impact.² Thus many were watching as the court determined whether to allow a company, Airgas, to redeem its poison pill to stop the bid of a would-be acquirer, Air Products.³

With only a small number of exceptions, Delaware courts have upheld pills (technically known as shareholder rights plans) as a legitimate defense against hostile takeovers since they first came into wide use in the 1980s. As recently as last year’s *craigslist* decision,⁴ the Delaware Supreme Court reaffirmed the idea that boards have wide discretion to adopt and implement poison pills. This is in line with the Delaware judiciary’s historical preference of deferring to the decision making of directors over shareholders.

This takeover battle spotlights the critical question of how far a board of directors of a Delaware corporation can go to get the price that it says the company is worth – making it a closely watched decision for shareholder activists. In upholding the legality of the poison pill, Chancellor Chandler framed the issue as:

[T]his case brings to the fore one of the most basic questions animating all of corporate law, which relates to the allocation of power between directors and stockholders. That is, when, if ever, will a board’s duty to ‘the corporation and its shareholders’ require [the board] to abandon concerns for ‘long term’ values (and other constituencies) and enter a current share value maximizing mode?

The 158-page opinion (with 514 footnotes) ultimately relies on the *Unocal* standard⁵ requiring board defensive action to be reasonable in relation to the threat posed, and found that an inadequately priced offer, even where un-coerced, was sufficiently threatening to justify the adoption of a poison pill.



POISON PILL: A defensive tactic used by a company that is a target of an unwanted takeover to make its shares or financial condition less attractive to an acquirer. For instance, a firm may issue a new series of preferred shares that give shareholders the right to compel their redemption at a premium price after a takeover. - *Black’s Law Dictionary*

FACTS, JUST THE FACTS

Air Products had an outstanding \$70-a-share, all-cash tender for all of Airgas’s outstanding stock but was blocked from consummating the acquisition by a poison pill. It had raised and extended its offer several times since first making it public in February 2010 and was rebuffed by the target corporation’s board of directors.

The target's board, including three directors hand-picked by the acquirer, insisted that the company was worth at least \$78 a share and contended that the pill is the only protection its shareholders have against an allegedly coercive offer. Each side had financial advisers supporting their position.

Judge Chandler of Delaware's Court of Chancery task was to decide whether Airgas would be justified in keeping its corporate defenses, even though a majority of its shareholders would like to accept the \$70 a share offer.

Last November, the Delaware Supreme Court refused to approve Air Product's proposed amendment that would have moved Airgas's next annual meeting up to January 2011, which would have shortened the term of the Airgas directors' terms by eight months. (Because three Air Products-nominated board members were voted in during the September 2010 board meeting, this decision was viewed as a significant win by Airgas.)

In this regard, it may be important to note that Airgas has a staggered board, sometimes referred to as a classified board, where shareholders only get to elect three or four directors each

year in a class, making hostile takeover attempts more difficult. However, Airgas shareholders have the right to call a special meeting to overturn the board, a capability possessed by only six of 85 Fortune 500 firms with staggered boards.⁶

TAKEAWAYS

The Airgas view of Delaware law, that "stockholders have the right to decide whether to sell their own individual shares, but they are not vested with the power to decide whether to sell the company as a whole,"⁷ has prevailed, to the chagrin of those who hold with the right of shareholders to ultimately control the companies they own. With merger and acquisition activity high, and litigation abounding, this decision provides additional certainty to both sides of the transaction.

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¹ "Air Products ruling will set benchmark in takeover battles," *Financial Times*, January 24, 2011, page 19.

² <http://corp.delaware.gov/> on January 30, 2011.

³ *In re Airgas Inc. Shareholder Litigation*, Civil Action No. 5249-CC.

⁴ *eBAY Domestic Holdings, Inc. v. Craig Newmark and James Buckmaster, craigslist, Inc.*, September 9, 2010.

⁵ *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985).

⁶ *Financial Times* article, referenced above.

⁷ From Airgas' brief as quoted in <http://dealbook.nytimes.com/2011/02/04/final-volleys-fired-over-the-airgas-poison-pill/>.