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TAKEOVERS AND TENDERS: A STOCK EXCHANGE VIEWPOINT

Remarks by Robert W. Haack, President, New York Stock Exchange, At The National Conference of The American Society of Corporate Secretaries. Fairmont Hotel, San Francisco, California, Tuesday Morning, June 17, 1969

I've been asked to discuss the policies of the New York Stock Exchange with respect to the securities of conglomerate corporations, and to comment on some of the problems we've been grappling with in this complicated and often confusing area. I hope, with your indulgence, that I can clarify some of the Exchange's views.

And I'd like to begin by tossing away the word, "conglomerate," which we never use at the Stock Exchange. Let me hasten to add that we have no quarrel with the conceptual definition of "conglomerate" adopted by the Financial Executives Institute. According to the Institute, a "conglomerate" is a company which is so managerially decentralized, so lacks operational integration, or has such diversified markets that it may experience rates of profitability, degrees of risk and opportunities for growth which vary considerably within the company -- so that an investor requires information about these variations in order to make informed decisions.

What we at the Exchange dislike about the term, "conglomerate," is the way it has been used by others --often in a strongly pejorative sense-- to suggest wider or narrower meanings. Consequently, we prefer to speak of multi-national companies, or multi-business companies, or companies with diversified operations -- depending upon the specific circumstances. I think it makes better sense to use these more precise terms to describe a particular company and its activities.

As you know, a number of specialized and highly complex techniques have been developed and used by companies seeking to diversify their

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activities through the acquisition of other companies. There has been, for example, a tremendous increase in the number of tender offers to stockholders by companies seeking to gain control of others.

EQUAL OPPORTUNITY FOR ALL STOCKHOLDERS

By and large, the Exchange's relations with listed companies engaging in these activities have centered on joint efforts to see that such offers are presented fairly and in accordance with good business practice. The vast majority of companies have indeed been extremely cooperative in this regard.

As a matter of policy, the Exchange does not comment on the merits of tender offers, or inject any subjective opinions into the often-vigorous corporate battles which sometimes result from them. Our policies in this area --which have developed over a period of some 15 years-- are based upon certain principles which we regard as fundamental.

Above all, we believe that all stockholders should have the opportunity to participate in a tender offer on equal terms. We believe that stockholders should be given sufficient time --preferably 30 days or more-- to decide whether or not they wish to accept an offer.

Frequently a company will limit the amount of a security covered by its tender offer. In such cases, we believe, the offer should remain open for a period of at least ten days to allow for the possibility that more shares may be offered than the company is prepared to accept. If that happens, the acceptance of shares should be pro-rated, so as not to exclude any stockholders signifying their desire to participate.

The so-called Williams Bill, enacted last year, had the effect of buttressing the Exchange's policies which, previously, lacked formal legal authority for enforcement. But that legislation by no means solved all the

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problems of fair and equal opportunity for all stockholders receiving tender offers. And, quite frankly, we sometimes find it necessary, in enforcing our policies, to insist that listed companies accept requirements more stringent than those set down by law.

An important case in point involves tender offers which are exempt from the provisions of the Williams Bill. The bill, as I'm certain most of you are aware, covers only cash offers, exempting securities offers registered under the 1933 Securities Act. We have been given to understand that, on a legal basis, an offer of securities need not be made on equal terms to all securities holders of a company which is the target of a takeover bid. Thus, the Exchange's policies come up against the legal possibility, in some instances, that institutions --for example-- could be favored over the general public.

And, indeed, some companies have wanted to offer institutions a cash premium over and above the amount of securities being offered. This is directly opposed to Stock Exchange policy, and we have insisted that any such premium must be offered to the non-institutional holder as well.

In all our rulings on tender offers involving Exchange-listed companies, the guiding principle --to reiterate a point about which we feel most strongly-- is that large and small stockholders should be offered equal terms for participation.

Interestingly enough, we have been accused in some cases of somehow favoring one side or the other. And there have been situations in which each side has accused us of favoring the other. I suspect that this may really be one of the surest ways of knowing that we have succeeded in our efforts to be impartial!

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TIMELY DISCLOSURE OF TERMS

Another matter with which we are very deeply concerned involves the preliminary planning of a tender offer. Great care should be taken to keep preliminary discussions confidential. But we have found that as soon as such information becomes known outside the top management echelon of the company or companies involved, there is inevitably the danger of a leak.

Incomplete or inaccurate information about a contemplated or pending offer can, of course, play havoc with investor confidence and, consequently, have an unsettling effect on the market. Thus, the Exchange insists that the participants recognize this and be prepared to disclose immediately --in such an event-- pertinent information as permitted under the prior registration requirement.

In one recent situation in which a leak did occur, the Exchange --with the concurrence of the managements of the companies on both sides of the pending offer-- suspended trading in the stocks of both companies for a day and a half. Both companies recognized that this was essential to protect the interests of their respective shareowners and of potential investors generally -- and they worked without respite for some 36 hours to prepare an accurate public statement on the terms of the forthcoming offer.

RESPONSIBILITIES OF TARGET COMPANIES

This brings me to another important point -- the responsibilities of companies which are the targets of tender offers. We all realize, of course, that companies frequently oppose takeover bids. Nevertheless, we believe at the Exchange that when a company does become the target of a tender offer, management is obliged to notify its stockholders that the offer is being made. Management may certainly document its vigorous

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opposition to an offer --or, as may be the case, its enthusiastic support-- and has no obligation to assist the offeror in any way. But management in all cases does have an obligation to acquaint all stockholders with the fact that an offer is being made.

It is sometimes very difficult to distinguish between a raid and a crusade, and it is certainly true that a takeover bid can, on occasion, be very beneficial to the stockholders of the target company. A great deal depends upon the viewpoint of the individual -- which may, of course, be very different from the viewpoint of management. And the Exchange's role in all such situations hinges not on siding with one company or the other -- but on trying to see that the stockholders have an adequate opportunity to make up their own minds about whether or not they wish to participate.

Many of you will recall that only a few years back there was a rash of rather vehement proxy battles -- some successful, others not so successful. And as times have changed, methods of doing things have also changed. Today, the takeover bid seems pretty much to have replaced the proxy fight as the principal instrument of corporate combat. And, not surprisingly, we have a whole new series of problems with which to contend.

DEFENSIVE TACTICS

In its role as a kind of watchdog of corporate democracy, the Exchange last year was disturbed to find a number of so-called "defensive tactics" developing in response to the growing number of takeover bids. Some of the techniques which began coming to our attention seemed clearly to violate the principles of corporate democracy which we believe are essential to building and maintaining a broad base of public ownership. And we have been particularly concerned about defensive procedures which --whatever their objectives-- would discriminate among shareowners on the basis of

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the relative sizes of their investments.

Our Board of Governors has not as yet adopted a formal policy in this area. However, last December, the Exchange wrote to the presidents and secretaries of all listed companies, soliciting their views on some of these tactics. One of the proposed ploys which aroused our concern was the suggestion that an 80 per cent favorable vote be required for a merger or similar transaction --involving a tender offer-- with a corporation owning more than 10 per cent of any class of the company's securities -- as opposed to 66-2/3 per cent approval under any other circumstances.

Another controversial tactic involved the proposal to create a small class of preferred stock, to be placed privately, which would have an 80 per cent vote requirement for any merger. Well, obviously, such an arrangement would permit the negation by a few holders friendly to management of any favorable action by the public holders of common stock.

Nor are these two examples of so-called "defensive tactics" the only ones which have come to our attention.

The Exchange has pointed out, with regard to listed companies, that an arrangement which could be applied uniformly to all transactions of similar nature and without regard to the parties involved, normally would not be regarded as objectionable.

On the other hand, any proposal which results either in discrimination against an existing substantial stockholder or in discouragement of anyone seeking to make a substantial investment, would appear to raise serious problems. Such a proposal could possibly conflict with the Exchange's philosophy of corporate democracy and stockholders' voting rights.

Over the years, the Exchange has insisted that all holders of common stock must have the right to vote in proportion to their ownership or

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equity in a corporation, on an equal basis with all other stockholders.

Certain states, on the other hand, have attempted to legislate so as to give the Board of Directors --rather than the stockholders-- the controlling voice in questions of corporate combination.

When we asked listed companies for suggestions concerning corporate defenses against unwelcome takeover bids, a few companies answered, in effect, that the Exchange should mind its own business and leave these matters to the state or federal legislators.

But the Exchange believes these matters are very much its business. The Exchange has a firm commitment to the interests of corporate democracy, and to maintaining quality markets for corporate securities. And we have no intention of walking away from that commitment.

As I pointed out earlier, a great many of the Exchange's requirements and agreements --both with member brokerage firms and listed corporations-- embody terms which are considerably more stringent than those prescribed by law. And it is unrealistic to expect that the same would not hold true when we come to grips with the knotty problems posed by some of these elaborate anti-takeover defense mechanisms.

"FUNNY MONEY" SECURITIES

One key to our philosophy may be found in our uncompromising attitude toward the issuance of non-voting common stock by listed corporations. Very few laws exist which prohibit such issues. Nevertheless, in the interests of corporate democracy, the Exchange, for more than 40 years, has refused to list non-voting common stock. All common stocks listed on the Exchange today --without exception-- carry the right to vote. Moreover, we will delist the voting common stock of any listed company which creates a class of non-voting common stock or fails to solicit proxies for meetings

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of its stockholders.

And in this connection, there is one other matter of serious concern to the Exchange --again, in the area of tender and exchange offers-- which I want to discuss with you.

We have become increasingly concerned about the various types of securities being issued in connection with certain tender and exchange offers -- what some Wall Street lexicographers have begun referring to as "funny money."

Some time ago, the Exchange reminded all listed companies of our long-standing refusal to list long-term warrants, because of the tangle of problems they tend to create. But this has not deterred some companies from devising other types of new issues which are equally unacceptable for listing. As a result, we are examining such issues even more intensively than in the past -- especially in the light of the issuing company's size, its capital structure, interest coverage, and results of its operations -- prior to granting any authorization for listing.

Under certain circumstances, I should point out, failure to obtain authority for listing new securities could result in the Exchange's consideration of delisting a company's common stock.

We have, in two recent instances, refused to list the bonds of two companies after finding, from the companies' own prospectuses that, on a pro forma basis, earnings before taxes would not be sufficient to cover the interest on the bonds being used for the purpose of the acquisitions.

We did not take steps in either case to delist the common stock of the companies involved. And we are hopeful, frankly, that now that our policies are widely known, we will never have to take such drastic action.

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TWO NEW POLICY STUDIES

I think we have made it abundantly clear that the Exchange is determined that securities issued for the purpose of acquiring or absorbing other companies must be soundly based. And we have two studies under way at present which should prove helpful.

One of these is aimed at formulating standards for the listing of bonds which will preclude companies from precipitating situations as dramatic as the ones in which interest coverage was not adequate even on a pro forma basis.

The second study is concerned with long-term warrants. The question facing us is this: At what point is a company's common stock no longer suitable for continued listing on the Exchange because of the dilution that would occur if the warrants were to be exercised? In other words, at what point would such warrants represent a serious threat of relegating the outstanding common stock to such a minority status that it would no longer be representative of the company?

There are cases where the prospective dilution of common stock can be measured at 200, 300 or 400 per cent. One possible solution may be to require that current stockholders should approve any issue of warrants which would bring the outstanding warrants to a point where they would more than equal the number of shares of common stock currently outstanding. In any case, some of the problems in these areas are so fundamental that great care must be exercised in finding the most satisfactory answers.

All of these problems are further complicated by the tremendous changes which have been taking place in the market itself -- and in the public's use of Stock Exchange facilities. Just a few points might be mentioned in the context of today's discussion:

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GROWTH OF NYSE STOCK LIST

Last year, original common stock listings on the NYSE totaled 96 -- second only to the 1929 record of 116-- while an additional 30 prospects for listing were acquired by or merged into existing listed companies. During the same period, we removed 98 common stock issues from our List --largely through mergers and consolidations-- for a net loss of two companies.

At the same time, however, the total size of the List increased by more than a billion and a half shares --an all-time record-- with only one-third of the total increase accounted for by new listings. Just a few weeks ago, the 14 billionth share was listed on the Exchange.

The substantial increase in shares listed --the total has doubled in little more than seven years-- has played an important part in enabling the Exchange to keep pace with the tremendous growth in both individual and institutional shareownership. And as you are all aware, the increase in institutional participation in the market has been perhaps the most significant development during the present decade.

As recently as 1966, only 4.5 per cent of NYSE reported volume was in blocks of 10,000 or more shares. In 1967, the percentage increased to 6.7. Last year, large blocks accounted for 10 per cent of reported volume -- nearly 300 million shares. And the trend is continuing. During the first three months of this year, blocks of 10,000 or more shares accounted for slightly more than 14 per cent of reported volume.

At the same time, the total number of individual shareowners also has mushroomed -- to an estimated total of 26.4 million at the start of 1969. We expect to publish the results of a new Census of Shareowners --the first full NYSE Census since 1965-- about a year from now. And we expect that

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the new Census will show a further increase in the number of Americans who own shares in our nation's corporations.

In the past, corporate secretaries have been of great assistance to the Exchange in assembling much of the data that go into the Census of Shareowners --often at the expense of considerable time and effort. Your cooperation has played an important part in making the Census the most authoritative study of its kind -- and one which has earned wide acceptance by business, labor and government. And as you might expect, we will be calling on you again for similar help with the 1970 Census, on which the preliminary work has already begun.

It is comforting to realize that, if past performance is any indication, we can certainly look forward to a continuing partnership --not only in this, but in so many important areas of mutual concern-- that will benefit the securities industry, the business community generally, and the vast and still-growing investing public.

Thank you very much.

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