Securities Law: Developments in Takeovers, Securities Fraud and Insider Trading in the Seventh Circuit

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During the 1980-81 term the United States Court of Appeals for the Seventh Circuit decided twelve cases involving securities law issues. The cases involved hostile takeover attempts, securities fraud and insider trading. Each of these three areas of securities law is previewed briefly below.

The legal duty of a target corporation's board of directors when faced with a hostile takeover attempt is unclear: should the board attempt to preserve the independence of the corporation, obtain the highest price possible from the bidder or seek another bidder who might offer a higher price? Four takeover cases before the Seventh Circuit this term gave the court the opportunity to further define the duties of the target corporation's directors.

Six securities fraud cases presented familiar issues involving rule 10b-5, which imposes liability for deceptive and fraudulent conduct in connection with the purchase or sale of a security. What constitutes a security for purposes of rule 10b-5 is an issue that courts have frequently had to address. The Seventh Circuit had to consider whether a loan participation agreement, the purchase of 100% of the stock of a corporation, and the purchase of all the minority shares by the majority shareholder of a corporation constituted the purchase or sale of a security. Private remedies under rule 10b-5 have been implied by the courts, but since there is no statute of limitations within rule 10b-5, courts, including the Seventh Circuit this term, have had to determine the appropriate limitation period.

Section 16(b) of the Securities Exchange Act of 1934, which imposes liability on corporate insiders for short-swing profits, provided the court an opportunity to consider when a sale actually occurs in a corporate merger and whether liability should be imposed where the short-swing sale occurred pursuant to court order.

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TAKEOVERS

During the 1980-81 term the Seventh Circuit decided four cases involving corporate takeover attempts. Before examining them in detail, it is helpful to review the basic forms of takeovers.

There are three methods by which one corporation can take control of another. The simplest method is through a proxy contest. Under this method, the bidding corporation, acting as a shareholder of the target corporation, seeks to convince the target corporation’s shareholders to vote for the bidder’s candidates for the target’s board of directors. This method requires very little capital investment but is also the least likely to succeed. Incumbent management can usually prevail in any proxy contest.

The second method that may be used to accomplish a takeover is an exchange offer. Under this method, the bidding corporation issues its own securities, common or preferred stock or bonds, in exchange for the target corporation’s outstanding shares. Since the bidding corporation is issuing new securities to accomplish the takeover, it must register these securities under federal and state laws. The registration process can be a slow one. At the federal level the Securities and Exchange Commission has the power to delay the offer until it is satisfied that the required prospectus meets with the approval of the staff. Delays in approval under state laws are not uncommon. In an exchange offer the target corporation shareholders have to determine the value of the securities being offered to them and decide whether to exchange their shares by selling them through the stock market or, if the exchange offer is for less than 100% of the target’s stock, by retaining their stock interest in the target.

The third takeover method is the cash tender offer. Under this

1. Panter v. Marshall Field & Co., 646 F.2d 271 (7th Cir. 1981); McDermott Inc. v. Wheelabrator-Frye, Inc., 649 F.2d 489 (7th Cir. 1980); Mite Corp. v Dixon, 633 F.2d 486 (7th Cir. 1980), prob. juris. noted, 451 U.S. 968 (1981); City Investing Co. v. Simcox, 633 F.2d 56 (7th Cir. 1980).
2. For a general discussion of proxy contests, see E. Aranow & H. Einhorn, Proxy Contests for Corporate Control (2d ed. 1968).
3. For a general discussion of exchange offers, see A. Fleischer, Tender Offers: Defenses, Responses and Planning (1981).
6. Hereinafter referred to as the SEC.
8. For a general discussion of cash tender offers, see 1 M. Lipton & E. Steinberger, Takeovers and Freezeouts (1978).
method, the bidder offers to pay cash to the target corporation’s shareholders in exchange for their shares. Tender offers, whether of the cash or stock exchange variety, normally involve a price higher than the current market value of the target’s shares. This premium is paid to induce the target shareholders to sell. The bidder is willing to offer a premium because of a belief that the target corporation’s shares are undervalued.

When a cash tender offer is announced, the market price of the target’s shares will normally increase to a point somewhat below the offering price. The target’s shareholders then are faced with the same decision as in an exchange offer: whether to sell their shares at the market price, tender their shares and wait to be paid or, if the offer is for less than 100% of the target’s shares, retain their stock interest in the target.

The decision whether to sell or tender is particularly difficult if the offer is for less than 100% of the shares. If more shares are tendered to the bidder than the bidder is seeking to buy, the Williams Act, which was passed by Congress in 1968 to regulate cash tender offers, requires that the bidder purchase the shares on a pro rata basis. This means that each shareholder who tenders stock will have a portion of his stock purchased by the bidder and a portion returned to him. It is therefore possible for a target shareholder to realize more money by selling all of his shares at the market price before the tender offer is completed.

The Williams Act prescribes that tender offers must be held open for a minimum of twenty days. This gives the target’s shareholders time to consider the offer and has the effect of giving the target board of directors twenty days in which to respond as a board to the tender offer. The Act also provides that shareholders may withdraw shares they have tendered within the first fifteen days after the offer is made.

One of the most vexing issues in takeovers is determining whether a target board’s activity under these circumstances is consistent with the fiduciary duty to be loyal to the interests of the shareholders. Because a takeover attempt presents a threat to the directors’ positions as directors, it raises the likelihood of a conflict with the shareholders’ interests. The cases before the Seventh Circuit this term involved three types of target board resistance to takeover attempts.

10. Id. § 78n(d)(6).
11. See note 165 infra.
Panter v. Marshall Field & Co.\textsuperscript{14} involved one type of resistance by the target board: a challenge of the takeover on the basis of alleged antitrust violations. A second method of resistance is the use of state anti-takeover statutes to slow down or stop an unwanted takeover bid. \textit{Mite Corp. v. Dixon}\textsuperscript{15} and \textit{City Investing Co. v. Simcox}\textsuperscript{16} gave the court an opportunity to consider the constitutional problems raised by these state statutes. A third method of resistance is for the target management to arrange a takeover by a more compatible company (a "white knight")\textsuperscript{17} that presumably will pay a higher price and be more inclined to preserve the positions of incumbent management. \textit{McDermott Inc. v. Wheelabrator-Frye, Inc.}\textsuperscript{18} is a case of this type.


\textit{Panter v. Marshall Field & Co.}\textsuperscript{19} involved an attempt by Carter Hawley Hale,\textsuperscript{20} a California corporation that operates retail stores, to acquire control of Marshall Field & Co. CHH moved to acquire control immediately after the death of Joseph Burnham, Field's chief executive officer. CHH overtures were rebuffed by Field's. On December 10, 1977, CHH informed Field's that if it did not agree to a takeover at $36 per share (Field's stock was then selling at $22 per share), CHH would commence a hostile takeover.\textsuperscript{21}

Field's then launched a series of defensive moves, beginning with a lawsuit filed on December 12, challenging the proposed CHH takeover on the ground that it violated antitrust laws.\textsuperscript{22} This was followed by a press release stating that it was in the best interests of the corporation and shareholders that Field's remain independent, a letter to shareholders (subsequently alleged to be deceptive) stating that the company's earnings had improved, the decision to acquire space in Houston to open a store that would compete with CHH's Neiman-Marcus store, and an agreement to acquire Liberty House stores in the Pacific Northwest that would compete with other CHH stores.\textsuperscript{23}

Despite having already publicly raised its \textit{proposed} offering price

\begin{itemize}
\item \textsuperscript{14} 646 F.2d 271 (7th Cir. 1981).
\item \textsuperscript{15} 633 F.2d 486 (7th Cir. 1980), \textit{prob. juris. noted.}, 451 U.S. 968 (1981).
\item \textsuperscript{16} 633 F.2d 56 (7th Cir. 1980).
\item \textsuperscript{17} \textit{See} note 151 \textit{infra.}
\item \textsuperscript{18} 649 F.2d 489 (7th Cir. 1980).
\item \textsuperscript{19} 646 F.2d 271 (7th Cir. 1981).
\item \textsuperscript{20} Hereinafter referred to as CHH.
\item \textsuperscript{21} 646 F.2d at 279.
\item \textsuperscript{22} \textit{Id.} at 290.
\item \textsuperscript{23} \textit{Id.} at 280-81.
\end{itemize}
to $42 per share, CHH withdrew its proposed tender offer because "the expansion program announced by Marshall Field . . . has created sufficient doubt about Marshall Field's earning potential."24 The stock market apparently shared CHH's doubts because the price of Field's stock plummeted to $19 per share after the CHH announcement.25 This put the market price at less than one-half of CHH's last proposed offer and lower than the $22 value at the time that CHH announced its first proposed offer.

Many of Field's shareholders, particularly those who had held their stock throughout the two-month period during which CHH was attempting to acquire Field's, were obviously disappointed. Nineteen shareholders filed suits seeking to hold the directors of Field's liable for depriving them of the opportunity to sell their shares at an amount significantly higher than market value.26

The district court, refusing to let the case go to the jury, granted the defendants' motion for a directed verdict at the close of the plaintiffs' presentation of evidence.27 A divided Seventh Circuit affirmed.28

The plaintiffs attacked the defendants' conduct under three theories: first, that the defendants had violated section 14(e) of the Williams Act,29 which regulates the conduct of parties involved in a tender offer; second, that the defendants had violated section 10(b)30 and rule 10b-5,31 the antifraud provisions of the Securities Exchange Act; and third, that the defendants had breached the fiduciary duties to the corporation that are imposed on them by state law.32

**Applicability of the Williams Act**

Section 14(e) of the Williams Act33 prohibits deceptive conduct "in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any

24. *Id.* at 281.
25. *Id.*
27. *Id.* at 1195.
28. 646 F.2d 271 (7th Cir. 1981).
32. The plaintiffs contended that the defendants breached their duties as corporate directors to both the corporation and its shareholders by: adopting a secret policy to resist acquisitions regardless of the benefit to the shareholders or the corporation; making defensive acquisitions; filing an antitrust suit against CHH; and interfering with the possible economic advantage to the shareholders, which caused CHH to withdraw its proposed tender offer before it became effective. 646 F.2d at 293.
such offer, request, or invitation."\textsuperscript{34} The \textit{Panter} majority, following the recent Second Circuit decision in \textit{Lewis v. McGraw},\textsuperscript{35} held that since no formal tender offer was made, section 14(e) was inapplicable.\textsuperscript{36} They reasoned that deceptive conduct could only be actionable if the plaintiffs could have relied upon it in deciding whether to tender shares to the bidder. Since there was no tender offeror, there could be no reliance.\textsuperscript{37} The majority decision is on solid ground since the purpose of the Williams Act is to insure that the target corporation's shareholders are provided with information needed to make an intelligent decision regarding the \textit{disposition} or \textit{retention} of their stock.\textsuperscript{38}

Judge Cudahy, in dissent, argued that the Williams Act could be applied to the kinds of pre-offer activity that took place in this situation.\textsuperscript{39} He expressed concern that the position of the majority "would have the effect of providing a safe harbor for target companies who were successful in their use of misstatements or deception to discourage the making of tender offers."\textsuperscript{40} The dissent thus implied that the effect of the majority's opinion will be to encourage deceptive statements by the target in the pre-offer period. However, other securities laws act as a powerful deterrent to the public issuance of deceptive statements by target corporations during the period prior to the effective date of a tender offer.\textsuperscript{41} Another problem with the dissent is that it ignores the fact that the Williams Act does not provide an explicit right to target corporation shareholders to sue for damages.\textsuperscript{42} The dissent assumes, without discussion, that shareholders have an implied right of action for damages under the Williams Act. This is not a safe assumption since the Supreme Court has not yet considered this issue. In \textit{Piper v.}}
Chris-Craft Industries, Inc.,\textsuperscript{43} the Court held that a defeated tender offeror lacked standing to sue for damages.\textsuperscript{44} While a number of lower federal courts have held that an implied right exists,\textsuperscript{45} the tone of the Supreme Court opinion in \textit{Piper} and other recent Court decisions "signal[s] . . . a retreat for the federal courts in securities regulation."\textsuperscript{46} The Court is increasingly reluctant to imply private rights under the federal securities laws. It has recently refused to imply a private right of action for damages under section 17(a) of the Securities Exchange Act\textsuperscript{47} and section 206 of the Investment Advisers Act of 1940.\textsuperscript{48}

In spite of the Court's reluctance to imply private rights of action, it may be willing, in some cases, to recognize such a right for target corporation shareholders because they are the primary class that the Williams Act seeks to protect.\textsuperscript{49} It is hard to believe, however, that the Court would be willing to imply such a right in a case like \textit{Panter} when no formal tender offer had occurred and the target corporation shareholders had not been confronted with the choice of whether to sell their shares in the market, tender to the tender offeror or retain their shares in the target corporation.

\textbf{Applicability of Rule 10b-5}

The plaintiffs' claims under rule 10b-5\textsuperscript{50} were brushed aside. Relying on the Supreme Court's decision in \textit{Santa Fe Industries, Inc. v. Green},\textsuperscript{51} the Seventh Circuit held that even if the plaintiffs' allegations were accepted—if the acts by Field's directors were actually deceptive—it would be a breach of state law fiduciary duty, but not a violation of rule 10b-5.\textsuperscript{52} It is not surprising that the court found no valid rule 10b-5 claim here. \textit{Santa Fe} makes it clear that where the core of the allegation is breach of state fiduciary duty, the plaintiff may not transform the complaint into a rule 10b-5 action merely by asserting that public statements or failures to make such statements constitute

\textsuperscript{43} 430 U.S. 1 (1977).
\textsuperscript{44} Id. at 47.
\textsuperscript{49} See Piper v. Chris-Craft Indus., Inc., 430 U.S. at 26.
\textsuperscript{50} 17 C.F.R. § 240.10b-5 (1981).
\textsuperscript{51} 430 U.S. 462 (1977).
\textsuperscript{52} 646 F.2d at 289.
The deceptive acts alleged in *Panter* were: (1) failure to disclose that the corporation had a secret policy of remaining independent at all costs; (2) failure to disclose that CHH’s original offer of $36 per share was merely a negotiating figure; (3) failure to disclose CHH’s willingness to cure any apparent antitrust problems; (4) failure to disclose true reasons for the hasty expansion into geographical areas in which CHH operated; and (5) misrepresentation of the company’s earnings. The majority held that the evidence did not support the plaintiffs’ assertion that these were deceptive acts. Judge Cudahy agreed as to the first four, but differed with the majority regarding the alleged misstatement of earnings. On December 20, 1977, the president of Field’s announced, in a letter to its shareholders, that earnings for the nine months ending October 31 were up 13%. In fact, earnings for the year turned out to be down 25%. The letter to shareholders said, in part:

> A number of programs to improve our profitability and expand our profit base were initiated . . . . Even at this early date, these programs are having positive effect. For example, we have disposed of most of our interest in The Ritz-Carlton hotel. This has eliminated a significant drain on our earnings. The revitalized merchandising programs are generating increased sales.

> —For the nine months ended October 31, income before ventures and taxes was up 24.4% and consolidated net income was up 13%.

At the time the letter was written, internal documents indicated a projected loss for the year of 7%. On its face, this suggests a knowing misstatement of a material fact in clear violation of rule 10b-5; nevertheless, the majority did not see it that way. It felt that the internal projections were too uncertain to allow public disclosure. The major-

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53. 430 U.S. at 478.
54. 646 F.2d at 288.
55. *Id.* at 289. The $36 figure was attacked as inadequate in public statements by Field’s. *Id.* at 290.
56. *Id.* The plaintiffs also alleged that Field’s failed to disclose two related facts: (1) that Field’s antitrust counsel was not present at the board meeting when it was decided to file the antitrust action; and (2) Field’s true motives in filing the lawsuit. *Id.*
57. *Id.* at 291.
58. *Id.* at 291-92.
59. *Id.* at 293.
60. *Id.* at 299 (Cudahy, J., dissenting).
61. *Id.* at 280.
62. *Id.* at 292.
63. *Id.* at 291-92 n.5.
64. *Id.* at 292.
65. The earnings projections were from a five-year plan hastily updated so the Field’s man-
ity argued that it was clear from the letter that "Field's earnings would be adversely affected in that fiscal year by the unprofitable ventures." Judge Cudahy, however, in finding a rule 10b-5 violation, stated that it is "just as rational to interpret the letter as saying that, but for the sour undertakings, the nine-month numbers would be even better." Indeed, it is difficult to understand how the majority reached its conclusion. According to the letter, the 24.4% increase in earnings is reduced by "ventures and taxes" to produce a 13% "consolidated net income." For the majority's interpretation to be correct, the 13% increase would have to be treated as consolidated net income before ventures—a very strained interpretation at best.

At the time this letter was written, Field's management knew that shareholders were deciding whether to retain their shares or sell their Field's stock into a rising market. This letter would seem to have been intended to affect decisions regarding the purchase and sale of Field's stock. It has the appearance of a classic rule 10b-5 violation; thus, it is difficult to believe that a letter such as this does not raise sufficient questions under rule 10b-5 to merit consideration by the jury.

Applicability of State Law

According to the majority, the critical issue was whether the directors were acting primarily in their own interests or in the interests of the shareholders. Field's stock was selling at $22 per share before CHH expressed interest. CHH's proposed tender offer was raised to $42 per share after an original suggestion of $36 per share. This would have represented almost a doubling in value of each share. Since the direc-

66. Id. at 292 n.5.
67. Id. at 312 (Cudahy, J., dissenting).
68. Id. at 292 n.5. See text accompanying note 63 supra.
69. The public announcement that CHH was willing to offer $36 per share caused the price of Field's stock to rise from $22 per share to over $28 per share. Field's shareholders had to decide whether to sell their shares at the market price, wait for a higher priced tender offer or hold their shares for long-term investment. See note 165 infra for a discussion of valuing a tender offer. Those who bought stock when the price was in the $28-$32 range were arbitrageurs—professional investors who purchase target corporation shares at less than the offering price and assume the risk of completion of the tender offer.
71. 646 F.2d at 296.
72. See text accompanying notes 24-25 supra.
tors are required by law to act in the best interests of the shareholders,\footnote{See, e.g., Wilderman v. Wilderman, 315 A.2d 610, 615 (Del. Ch. 1974); Harmony Way Bridge Co. v. Leathers, 353 Ill. 378, 395, 187 N.E. 432, 439 (1933).} what is the basis for deciding that they were justified in resisting the CHH approach?

The majority, looking to Delaware law because Field's is a Delaware corporation, found that the Delaware business judgment rule insulated the directors from liability.\footnote{646 F.2d at 293.} They cited with approval the district court's statement that

\[\text{[d]irectors of corporations discharge their fiduciary duties when in good faith they exercise business judgment in making decisions regarding the corporation. When they act in good faith they enjoy a presumption of sound business judgment, reposed in them as directors, which courts will not disturb if any rational business purpose can be attributed to their decisions. In the absence of fraud, bad faith, gross overreaching or abuse of discretion, courts will not interfere with the exercise of business judgment by corporate directors.}\footnote{Id. (quoting 486 F. Supp. 1168, 1194 (N.D. Ill. 1980) (citations omitted)).}

Judge Cudahy challenged the application of the rule to tender offers.\footnote{646 F.2d at 300 (Cudahy, J., dissenting).} He contended that the business judgment rule is intended to insulate directors from liability regarding decisions made in managing the business enterprise because directors are presumed to have more expertise than shareholders in making such decisions; no such presumption is warranted, however, with regard to a tender offer, particularly since there is a strong self-interest on the part of directors to remain in office.\footnote{Id at 294.}

The majority held that the plaintiffs could prevail only if they introduced evidence "from which a factfinder might infer that impermissible motives predominated in the making of the decision in question."\footnote{Id. at 300 (Cudahy, J., dissenting).} The presence of a majority of independent members on the Field's board was the basis for a "heightened"\footnote{Id. at 294.} presumption of good faith on the part of the board. Judge Cudahy argued that the mere fact that a majority of the board was not directly on Field's payroll did not prove a lack of self-interest. At a minimum, he noted, they were interested in "their own positions of power, prestige and prominence" as well as "defending against outside attack the management which they have . . . installed in power."\footnote{Id. at 300 (Cudahy, J., dissenting).}
The majority placed considerable emphasis on whether the directors were acting to protect the shareholders and the corporation from injury. 81 What injury to the shareholders could there have been? Foregoing the opportunity to receive more than $42 per share? Certainly there was no evidence that anyone else thought that Field's was worth that much. Nor has the subsequent performance of the stock indicated a likelihood that the shareholders are going to see that price level again soon. 82 This was not a situation like that faced by Conoco, Inc. when it recently resisted a $65 per share offer because of management's belief that the corporation was worth much more—a belief demonstrated shortly thereafter. 83

How else could the corporation or its shareholders have been injured? The majority suggested that the filing of the antitrust suit "clearly served the rational business purpose of protecting Field’s from the damage forced divestiture would cause." 84 No authority was cited for this proposition. It seems reasonably clear that the Field’s shareholders would have had no liability if the acquisition was later deemed to have violated the antitrust laws. 85 If at some future date CHH was forced to divest itself of Field’s, that could not adversely affect the current Field’s shareholders—they would already have received their $42 per share. Only CHH’s shareholders would be in a position to be adversely affected.

The plaintiffs argued that the acquisition of stores in the Pacific Northwest and Houston was primarily motivated by a desire to create antitrust problems. The majority dismissed this argument, saying that such expansion was "reasonable and natural" and that the plaintiffs had failed to introduce any "evidence of bad faith, overreaching, self-dealing or any other fraud." 86 Judge Cudahy believed that there was more than ample evidence for a jury to conclude that it was not "reasonable and natural" for the directors of a major retailer to make expansion commitments totaling more than $40 million dollars [sic] during and shortly after a

81. Id. at 294.
82. As the court noted, Field's stock had dropped to $19 per share after CHH abandoned its proposed offer. Id. at 281. Almost four years later, Field's stock was even lower, closing at 14 1/4 on September 11, 1981. The Wall Street Journal, Sept. 14, 1981, at 46, col. 5. See note 285 infra.
83. The rejection of the $65 per share offer touched off a major contest for control that saw bidding reach $120 per share. See Smith, The Making of the Megamerger, FORTUNE, Sept. 7, 1981, at 58, 61, 64.
84. 646 F.2d at 297.
85. See Easterbrook & Fischel, The Proper Role of a Target's Management in Responding to a Tender Offer, 94 HARV. L. REV. 1161, 1192 n.91 (1981) [hereinafter cited as Easterbrook & Fischel].
86. 646 F.2d at 297.
busy Christmas season in which their "top priority" was to help a
ew chief executive officer become familiar with Field's operation.
Particularly when considered with the evidence of a long-standing
and uncompromising policy of independence, I am astonished that
the business judgment rule under any guise could keep this case from
the jury.\textsuperscript{87}

Judge Cudahy's belief that Field's had a long-standing policy of main-
taining its corporate independence was supported by evidence showing
that Field's had responded to three other proposed takeovers in the
past five years by making defensive acquisitions in the potential ac-
querr's operating territory.\textsuperscript{88}

It is difficult to believe that a Delaware court would agree with the
majority's interpretation of the Delaware business judgment rule. As
Judge Rosenn of the Third Circuit has noted, "Recent Delaware cases
reveal a growing trend to impose stricter obligations on management to
justify control-related transactions."\textsuperscript{89} The conduct of directors when
faced by a potential takeover is certainly "control-related." Of particu-
lar interest is the recent Delaware decision in \textit{Zapata Corp. v. Maldo-
nado}\textsuperscript{90} in which the court had to decide whether the business judgment
rule permitted the board of directors to dismiss a derivative suit. Nor-
mafly, the determination of whether a suit should be instituted or main-
tained is a business judgment to be made by the directors.\textsuperscript{91} In \textit{Zapata},
however, the directors of the corporation were the defendants. The de-
cision to dismiss the suit was made by an ostensibly independent com-
mittee made up of directors who had been appointed after the alleged
breach of fiduciary duty had occurred.\textsuperscript{92} The court refused to allow
dismissal of the suit without a determination that the nondefendant di-
rectors were truly exercising independent judgment.\textsuperscript{93} The court was
obviously concerned about whether the directors who voted to dismiss
the suit were exercising independent business judgment or merely seek-
ing to serve the personal interests of the other directors. This same
concern is present in \textit{Panter}. Were the Field's directors acting in their
own personal interests or were they truly exercising independent busi-
ness judgment? It is questionable whether a Delaware court after
\textit{Zapata} would acquiesce in Field's directors' business judgment claim

\textsuperscript{87} \textit{Id.} at 308-09 (footnote omitted) (Cudahy, J., dissenting).
\textsuperscript{88} \textit{Id.} at 305-06.
\textsuperscript{89} Johnson v. Trueblood, 629 F.2d 287, 301 (3d Cir. 1980) (Rosenn, J., concurring in part
and dissenting in part).
\textsuperscript{90} 413 A.2d 1251 (Del. Ch. 1980).
\textsuperscript{91} \textit{Id.} at 1256.
\textsuperscript{92} \textit{Id.} at 1254-55.
\textsuperscript{93} \textit{Id.} at 1263.
where the personal interest of the directors is significant and the business advantage to the corporation is doubtful.94

State Takeover Legislation

Mite Corp. v. Dixon

The limits of state authority to regulate the takeover of publicly held corporations was the central issue faced by the Seventh Circuit this term in Mite Corp. v. Dixon.95 On January 19, 1979, Mite, through a wholly-owned subsidiary, filed the appropriate documents with the SEC96 to commence a tender offer for all of the shares of Chicago Rivet & Machine Company. The offering price was $28 per share for stock that was then selling at $24 per share.97 On the same day that it filed with the SEC, Mite commenced an action in federal district court seeking to enjoin the Illinois Secretary of State from enforcing the Illinois Business Take-Over Act98 and seeking to have the Illinois Act declared unconstitutional under the supremacy and commerce clauses of the United States Constitution because of a conflict with the Williams Act.99

On February 1, the Illinois Secretary of State notified Mite100 that he intended to issue a temporary cease and desist order prohibiting Mite from proceeding with its tender offer for failure to comply with the filing requirements of the Illinois Act. The following day, the district court temporarily enjoined the Secretary of State from enforcing the Illinois Act101 and a week later the injunction was made perma-

94. There are also persuasive arguments that economic efficiency and shareholder welfare would be maximized by sharply limiting the defensive measures that directors are permitted to take when faced with a hostile tender offer. Professors Easterbrook and Fischel have recently argued that the value of all equity investments in public corporations would increase if target corporation directors were required to maintain a passive role in takeover situations. Easterbrook & Fischel, supra note 85, at 1201-02.
97. 633 F.2d at 488.
99. 633 F.2d at 488.
100. Chicago Rivet had moved to dismiss Mite's challenge of the Illinois Act on the ground that no case or controversy existed between the parties. It did not intend to invoke the Illinois Act against Mite and Secretary of State Alan Dixon was undecided whether Mite's offer was nevertheless exempt under the Illinois Act. The federal district court ordered Mite's request for injunctive relief continued until further notice and ordered both Chicago Rivet and Secretary Dixon to inform Mite in writing of any future intention to act against Mite. Id. at 489. This February 1 notification was pursuant to that order.
101. Once Secretary Dixon was stopped from issuing a cease and desist order, Mite published in The Wall Street Journal its offer to buy stock of Chicago Rivet. The offer was made to Chicago
The Secretary of State appealed to the Seventh Circuit which affirmed the district court's decision declaring that the Illinois Act was in conflict with both the supremacy and commerce clauses of the Constitution.

The supremacy clause violation resulted from a fundamental philosophical conflict between the Illinois Act and the Williams Act. The latter requires that information be furnished to the target's shareholders so that they may make a decision on the merits. The Illinois Act provides for the state initially to determine the substantive fairness of the tender offer. As the court noted, "this approach to investor protection by 'benevolent bureaucracy' is preempted by the conflicting approach of the Williams Act, which contemplates unfettered choice by well-informed investors." Since the Williams Act does not explicitly or implicitly prohibit all state regulation of securities, the court had to carefully analyze the conflict between the two acts. The fundamental conflict, both philosophical and practical, was apparent from a number of specific provisions of the acts. The Williams Act provides for disclosure of information upon commencement of an offer, a minimum twenty-day period in which an offer must be held open, a fifteen-day period in which shareholders may withdraw tendered shares and a requirement that the offeror purchase shares on a pro rata basis when not purchasing all shares tendered. The Act does

Rivet's shareholders throughout the United States; the transaction would have been in excess of $23,000,000. Id.

102. Id. The injunction declared that the Illinois Act was preempted by the Williams Act and was an unconstitutional burden on interstate commerce.

103. Mite withdrew its tender offer; nevertheless, the case was not mooted because if the Seventh Circuit reversed the district court's order, Mite would have been subject to civil and criminal penalties under the Illinois Act. Id. at 490.

104. Id. at 488.
106. ILL. REV. STAT. ch. 121½, § 137.57(A) (1979).
107. 633 F.2d at 494.
108. Section 28(a) of the Securities Exchange Act of 1934 provides:

Nothing in this chapter shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this chapter or the rules and regulations thereunder.


The Fifth Circuit, in Great Western United Corp. v. Kidwell, 577 F.2d 1256 (5th Cir. 1978), rev'd on other grounds sub nom. Leroy v. Great Western United Corp., 443 U.S. 173 (1979), said that the purpose of § 28 was to preserve state blue sky laws and it probably does not apply to the Williams Act. 577 F.2d at 1275 n.39.

111. Id. § 240.14d-7(a)(1).
not provide for a hearing or a determination of fairness of the terms of the offer. The shareholders make that decision themselves.

The Illinois Act provides for a twenty-day notice before commencing an offer.\(^{113}\) This notice probably constitutes commencement of an offer under the Williams Act, making the two acts procedurally in conflict. The Illinois Act further provides that a hearing to determine the substantive fairness of the offer be held if the Secretary of State receives a written request for a hearing within fifteen days after the prospective tender offeror files the required registration statement.\(^{114}\) The request for a hearing must be submitted by a majority of the independent (non-employee) directors of the target corporation or the owners of 10\% or more of the target corporation stock.\(^{115}\) Thus, the Illinois Act effectively gives incumbent management the power to force a hearing because "in a significant number of cases management will be able to use the provision, either through its ability to influence outside directors, or because it will, directly or indirectly, exercise some (or a great deal of) control over the required number of outstanding shares."\(^{116}\)

The decision in \textit{Mite} will provide the United States Supreme Court, which has noted jurisdiction of the appeal,\(^{117}\) with the opportunity to settle a controversy that has intensified in recent years.\(^{118}\) More than two-thirds of the states have enacted takeover statutes similar to the one in Illinois.\(^{119}\) Before these statutes were enacted, most cash tender offers were consummated ten days after announcement.\(^{120}\) The state statutes have the effect of increasing the time it takes to complete a tender offer. This allows target companies more time to take defensive measures to avoid takeovers.\(^{121}\) The potential for significant delay in purchases of securities from shareholders residing in states other than Illinois was the major reason that the Seventh Circuit found the Illinois Act to be an unreasonable burden on interstate commerce. "[I]n making the 'delicate adjustment' of state and federal claims"\(^{122}\) the court was unimpressed with Illinois' claimed interests in regulating take-

\(^{113}\) \textsc{Ill. Rev. Stat.} ch. 121-1/2, § 137.54(E) (1979).
\(^{114}\) \textit{Id}. § 137.57(A).
\(^{115}\) \textit{Id}.
\(^{116}\) 633 F.2d at 495.
\(^{119}\) \textit{Id}. at 441.
\(^{120}\) \textit{Id}. at 440.
\(^{121}\) \textit{Id}. at 441-42.
\(^{122}\) 633 F.2d at 500.
overs. The supposed interest in protecting shareholders was deemed "speculative," particularly since the act could apply even if there were no Illinois shareholders. The court also expressed the view that in at least some circumstances the Illinois Act could be "detrimental to the interests of the shareholders." The other claimed interest of the state was in regulating the internal affairs of corporations organized under Illinois law. The court expressed doubt as to whether the sale of stock from one investor to another is truly a matter of internal corporate affairs. However, the court said, even if it is viewed as such, Illinois showed no specific reason why this interest should be asserted in this case. Furthermore, the statute applies to corporations that are not incorporated in Illinois and the state obviously can make no such claim in those cases. The broad jurisdictional reach of the Illinois Act also suggests that other states with similar statutes might assert an interest in regulating the same tender offer. Indeed, at one point in this case, Chicago Rivet unsuccessfully attempted to invoke the Pennsylvania takeover statute.

A tender offer aimed at the shareholders of a publicly held corporation is often a national event. Permitting several states to regulate part or all of an offer would potentially destroy tender offers which are an important tool for maintaining economic efficiency of corporations and enhancing shareholder wealth.

*City Investing Co. v. Simcox*

Another case involving the limits of state regulation of takeovers was *City Investing Co. v. Simcox*. City Investing, a Delaware corporation, made open market purchases of 5.1% of the common stock of Stokely-Van Camp Inc., an Indiana corporation. City Investing filed the required Schedule 13D under the SEC rules, indicating an intent to eventually buy 15% to 20% of Stokely stock for investment purposes. Shortly after City Investing filed its Schedule 13D, the Indiana Commissioner of Securities began proceedings under the Indiana

123. *Id.*
124. *Id.*
125. *Id.* at 501.
126. *Id.*
127. *Id.* at 502.
128. *Id.*
129. *Id.* at 488-89.
130. See Easterbrook & Fischel, *supra* note 85, at 1173.
131. 633 F.2d 56 (7th Cir. 1980).
133. 633 F.2d at 57.
Takeover Offers Act\textsuperscript{134} and issued a cease and desist order.\textsuperscript{135} 

City Investing brought suit in federal district court seeking to have the Indiana Act declared unconstitutional. The district court's decision,\textsuperscript{136} affirmed by the Seventh Circuit,\textsuperscript{137} was to abstain from deciding the question because of a potentially dispositive state law issue.\textsuperscript{138} The Seventh Circuit expressed doubt that the Indiana Act applies to open market purchases since such purchases do not appear to constitute a tender offer within the meaning of the Act.\textsuperscript{139} The court strongly implied that the Indiana courts would overturn the Commissioner's decision to challenge City Investing's open market purchases because his decision "has all of the earmarks of a 'hometown call.'"\textsuperscript{140} If the Indiana courts were to uphold the Commissioner's assertion of jurisdiction over City Investing's purchases, the Indiana Act would most certainly be found unconstitutional on the same basis as the Illinois Act.\textsuperscript{141} 

The Seventh Circuit's assumption that Indiana would not define open market purchases as a tender offer may be incorrect. While open market purchases do not constitute a tender offer under the Williams Act, it cannot be assumed that state statutes will be similarly interpreted. Indeed, the New Hampshire Supreme Court recently decided that open market purchases for control can constitute a tender offer.\textsuperscript{142} 

It seems clear that the present array of state statutes cannot be permitted to remain in force. It would not be surprising if the Supreme Court takes the opportunity presented by \textit{Mite} to declare these state takeover statutes unconstitutional. However, even if the Court does affirm the Seventh Circuit's decision in \textit{Mite}, there is likely to be additional legislative activity on this subject. There are presently a number of legislative and regulatory efforts under way to insure that the national character of tender offers is recognized. The SEC has asked Congress to explicitly preempt all state regulation of tender offers.\textsuperscript{143} In addition, the SEC has amended the Williams Act regulations in or-

\textsuperscript{136} 476 F. Supp. 112 (S.D. Ind. 1979). 
\textsuperscript{137} 633 F.2d 56 (7th Cir. 1980). 
\textsuperscript{138} 476 F. Supp. at 115-16. 
\textsuperscript{139} 633 F.2d at 60-61. 
\textsuperscript{140} \textit{Id.} at 61. 
\textsuperscript{141} \textit{See} \textit{id.} at 61-62. 
\textsuperscript{142} \textit{See} Sharon Steel Corp. v. Whaland, 433 A.2d 1250 (N.H. 1981). 
\textsuperscript{143} \textit{See} Proposed Bill to Amend Williams Act, § 28(a), 542 SEC. REG. & L. REP. (BNA) Spec. Supp. 29 (Feb. 27, 1980).
der to dramatize the conflict with the state statutes.\textsuperscript{144}

The American Law Institute's proposed Federal Securities Code\textsuperscript{145} recognizes the national character of tender offers and preempts state regulation unless the state has an obviously overriding interest in regulating the tender offer. The Code permits a state to regulate the tender offer if the target has its principal place of business within the state and more than 50\% of the shares are owned by residents of the state.\textsuperscript{146}

The proposed State Uniform Take-Over Act,\textsuperscript{147} adopted by the North American Securities Administrators Association, also recognizes the national character of tender offers by eliminating the possibility of more than one state regulating a takeover. The Act permits only the state of incorporation to regulate tender offers and provides that the state may further restrict the application of its law to corporations that have a specified percentage of shares owned by residents of the state.\textsuperscript{148} As the court stated in \textit{Mite}, the constitutionality of this type of statute probably depends upon the target having a significant percentage of shareholders residing in the state. All of these efforts suggest that the present takeover statutes will soon pass from the scene.

\textit{Amendment of Tender Offers: McDermott Inc. v. Wheelabrator-Frye, Inc.}

In \textit{McDermott Inc. v. Wheelabrator-Frye, Inc.},\textsuperscript{149} the contest for control of Pullman Inc. provided the court with an opportunity to decide a narrow but important question under the Williams Act: whether an increase in the number of shares sought by a tender offeror requires an extension of the time period that the offer must be held open. Pullman became the target of a contest for control between McDermott Inc. and Wheelabrator-Frye, Inc.\textsuperscript{150} WFI played the role of "white knight"\textsuperscript{151} and ultimately prevailed. Rule 14e-1 requires that tender

\textsuperscript{144} Rule 14d-2, 17 C.F.R. \textsection 240.14d-2 (1981), adopted November 29, 1979, provides that Williams Act disclosure requirements must be met within five days of the announcement of the number of shares sought, price, and identity of the target. The SEC has taken the position that a filing under state statutes is a public announcement. SEC Rel. No. 34-16384 [1979-1980 Transfer Binder] \textit{Fed. Sec. L. Rep. (CCH)} \textsection 82,373, at 82,584.

\textsuperscript{145} \textit{ALI Fed. Sec. Code (Mar. 1978 Draft)}.

\textsuperscript{146} \textit{Id.} \textsection 1904(c), at 715.

\textsuperscript{147} [1981] \textit{1 Blue Sky L. Rep. (CCH)} \textsection 5295.

\textsuperscript{148} \textit{Id.} \textsection 3(j).

\textsuperscript{149} 649 F.2d 489 (7th Cir. 1980).

\textsuperscript{150} Hereinafter referred to as WFI.

\textsuperscript{151} A "white knight" is a competing offeror friendly to the target corporation which attempts to "save" the target from being acquired by an offeror whose offer is considered undesirable by the target's board of directors. Fogelson, Wenig & Friedman, \textit{Changing the Takeover Game: The
offers remain open for a minimum of twenty days.\textsuperscript{152} In the battle for Pullman, WFI amended its offer on the twentieth day to increase the number of shares it was willing to buy. The dispositive issue in the case was whether the amendment constituted a new offer which would require that the offer be held open an additional twenty days.

The district court held that the Pullman shareholders did not have sufficient time to consider the amendment to the offer and granted McDermott's request to compel extension of the offer for an additional twenty-day period.\textsuperscript{153} A divided Seventh Circuit reversed.\textsuperscript{154}

The court was presented with two issues: first, whether a competing tender offeror has standing to seek injunctive relief and, second, whether the district court was correct in extending the time period of the offer. The majority avoided the first issue by reversing the district court's decision on the second issue.\textsuperscript{155} The majority treated the district judge's decision as a determination that WFI had made a new tender offer requiring the running of a new twenty-day period.\textsuperscript{156} They found this view inconsistent with rule 14e-1(b)\textsuperscript{157} which requires a ten-day extension of a tender offer when there is an increase in the price offered per share.\textsuperscript{158} The majority implied that if the SEC thought that an increase in the number of shares sought required extension of the tender offer, it would have provided a rule similar to rule 14e-1(b).\textsuperscript{159}

In his dissent, Judge Pell did find that very intent on the part of the SEC in rule 14d-4(c),\textsuperscript{160} "which requires that a 'material change' in the terms of a tender offer 'shall be promptly disseminated to security holders in a manner reasonably designed to inform security holders of such change.'" He agreed with the SEC's position, expressed in its amicus brief, that a period of only hours was not sufficient time for the shareholders to be reasonably informed and therefore an extension of five days might be reasonable, although he did not specifically suggest an appropriate time period.\textsuperscript{162} The majority rejected this argument but

\begin{align*}
153. & 649 F.2d at 491. \\
154. & 649 F.2d 489 (7th Cir. 1980). \\
155. & \textit{Id.} at 493 n.8. \\
156. & \textit{Id.} at 492. \\
158. & 649 F.2d at 492. \\
159. & \textit{Id.} \\
161. & 649 F.2d at 494 (Pell, J., dissenting) (quoting 17 C.F.R. § 240.14d-4(c) (1981)). \\
162. & 649 F.2d at 495. 
\end{align*}
stated that if Judge Pell was correct in finding rule 14d-4(c) applicable, sufficient time had already passed for the Pullman shareholders to evaluate the offer.163

The financial significance of WFI increasing the number of shares it was obligated to buy from 3,000,000 to 5,500,000 can readily be seen. This represented an increased expenditure of $131,250,000 and an increase in the percentage of stock sought from 27% to 49%.164 The relationship between the number of shares being sought and the outcome of a contested tender offer can be seen by viewing how the contest progressed on September 19. At the start of that day an estimated 3,882,000 shares had been tendered to McDermott at $43.50 per share. Only 1,000,000 shares had been tendered to WFI, even though it was offering $52.50 per share. The reason for the difference was that WFI was only committed to buy 3,000,000 shares (with an option to take 1,000,000 more), while McDermott was committed to buy 5,400,000. The lower priced McDermott offer was more attractive because Pullman shareholders estimated that the greater likelihood of their shares being accepted by McDermott made the actual value of the McDermott offer greater than the WFI offer. However, once WFI announced that it was willing to accept 5,500,000 shares at $52.50, the value of the offer dramatically changed and, by the end of the day, 7,300,000 shares had been tendered to WFI and almost all shares previously tendered to McDermott had been withdrawn. McDermott's increase in its offering price to $54 per share at 2:00 P.M. on the same day was inadequate to stem the flow of shares to WFI.165

There is no doubt that the dissent is correct in concluding that a

163. *Id.* at 493.
164. *See id.* at 491.
165. The value of the tender offer package to an investor who owns 100 shares might be calculated as follows:

\[
\text{Percentage of shares tendered likely to be purchased by tender offeror (PCT) } \times \text{ Number of shares owned by shareholder (N) } \times \text{ Per share offer price (P) } + \text{ Estimated residual value of shares not acquired by tender offeror (RV)} = \text{ Gross value of tender offer (GVT).}
\]

GVT should be multiplied by probability (PR) that tender offeror will be able to complete purchase on terms offered.

Application of this formula to the Pullman contest suggests this result:

**WFI offer**

\[
PCT (11,150,000 + 5,500,000) = 49.3 \times N (100) \times P (52.50) + RV (50.7 \times 40) = \text{GVT $4616.25 } \times \text{ PR .95 (WFI was the white knight and therefore there was a very high probability that the offer would succeed)} = $4385.4875.
\]

**McDermott offer**

\[
PCT (11,150,000 + 5,400,000) = 48.4 \times N (100) \times P (54.00) + RV (51.6 \times 40) (\text{assumes the same RV under both offers}) = \text{GVT $4677.60 } \times \text{ PR .80 (the opposition of the target and the presence of the white knight lower the probability of success)} = $3742.08.
\]
change in the number of shares sought can be at least as significant as an increase in the price offered. However, since takeovers are regulated by highly detailed rules, the SEC's failure to explicitly require an extension under these circumstances led the majority to implicitly defer to the SEC's "expertise." 166 The SEC's amicus brief, however, supported Judge Pell's dissent. For reasons that are not clear, the SEC has failed to promulgate a rule to cover this problem. Instead, it has submitted legislation to Congress that would require a ten-day extension of a tender offer when the tender offeror increases the number of shares sought.167

As noted earlier,168 the majority avoided the question of McDermott's standing to seek injunctive relief under the Williams Act. The dissent merely assumed its existence without discussion. However, there is still some doubt as to whether a competing tender offeror has such standing. In Piper v. Chris-Craft Industries, Inc. 169 the Supreme Court held that a competing tender offeror lacked standing to sue for damages.170 The Court reserved the issue of whether a competing tender offeror could seek injunctive relief.171 Allowing competing tender offerors to obtain injunctive relief is an effective way to help insure that target corporation shareholders receive the disclosure required by the Williams Act. To this end, the SEC has submitted legislation to Congress that would grant standing to competing tender offerors.172

Securities Fraud

Section 10(b) of the Securities Exchange Act of 1934173 and rule 10b-5174 promulgated under it prohibit fraud "in connection with the purchase and sale of a security."175 For many years, rule 10b-5 was

interpreted very broadly and a wide range of activities was brought within its scope. In the past five years the Supreme Court has limited the reach of rule 10b-5 by restricting actions under the rule to actual purchasers and sellers, excluding actions predicated on breaches of state fiduciary duties and requiring scienter as a prerequisite for liability.

During the 1980-81 term the Seventh Circuit decided six cases that raised issues under rule 10b-5. With one possible exception, the court’s decisions were in keeping with the restrictive tone of recent Supreme Court decisions. The rule 10b-5 cases considered by the Seventh Circuit dealt with four major issues: first, whether particular financial instruments satisfied the definition of a “security” for purposes of rule 10b-5; second, what constitutes a sufficient causal nexus to satisfy the “in connection with” requirement of rule 10b-5; third, how to determine the appropriate statute of limitations under rule 10b-5; and fourth, whether a brokerage firm could be held vicariously liable for a rule 10b-5 violation committed by one of its employees.

Definition of a Security

The meaning of the term “security” under the Securities Act of 1933 and the Securities Exchange Act of 1934 has been the subject of frequent litigation. The definition of a security under both acts includes an “investment contract,” a term that has been viewed as a “catch-all” to include new forms of financing that serve the same economic purpose as a security.
In *SEC v. W.J. Howey Co.* the Supreme Court defined an investment contract as "a contract, transaction or scheme whereby a person [1] invests his money [2] in a common enterprise and [3] is led to expect profits solely from the efforts of the promoter or a third party." In *United Housing Foundation, Inc. v. Forman,* the Court extended *Howey* by holding that ‘form should be disregarded for substance and the emphasis should be on economic reality.’ *Howey* required that an “investment contract” satisfy three requirements in order to be a security. *Forman* said that all securities, not just investment contracts, must meet the *Howey* test. Thus, in *Forman,* “stock” in a nonprofit cooperative housing corporation was held not to be a security since the economic substance was the purchase of an apartment and the money paid for the stock was in effect a security deposit. *Forman* created the opportunity for increased litigation about what constitutes a security because financial instruments that meet the facial definition of “security” are now subject to judicial scrutiny.

The Seventh Circuit decided three cases in which the financial instrument involved satisfied the literal definition of a security but nonetheless required careful examination on the basis of *Forman.*

In *American Fletcher Mortgage Co. v. U.S. Steel Credit Corp.*, the court had to decide whether the sale of a 40% participation in a mortgage loan was a security. American Fletcher, a mortgage banking company, agreed to loan $5,800,000 to Justin Development Corporation to finance construction of residential condominiums. American Fletcher then obtained loan participations from three financial institutions for the full $5,800,000. The three participating institutions were to be repaid principal and interest by Justin in proportion to their share of the loans. (In a loan participation, the lead bank, in this case American Fletcher, loans money directly to the borrower, is the payee of the borrower’s note, holds all collateral and manages the loan.) One of the participating institutions, U.S. Steel Credit Corporation, with 40% participation in the loan, had serious disagreements with Ameri-
can Fletcher about the project. After American Fletcher instituted suit for breach of contract, Steel filed a counterclaim in which it asserted that its loan participation was a security and that American Fletcher had made misrepresentations in connection with its sale, thereby violating the 10b-5.

Although a "note" is technically a security under both the Securities Act of 1933 and the Securities Exchange Act of 1934, both parties agreed that the note given to American Fletcher by Justin was not itself a security because American Fletcher was not making an investment within the meaning of the acts. Both parties also agreed that loan participations could be securities even if the underlying notes were not. Section 3(a)(10) of the Securities Exchange Act of 1934 includes in the definition of a security any "certificate of interest or participation in any profit-sharing agreement." The participation involved in American Fletcher could easily be viewed as a profit-sharing agreement, thus satisfying the literal definition of a security.

Applying the three-element analysis of Howey, however, the court held that the loan participations were not securities. The court said that, while there was an investment of money in a "common venture," the third element of the Howey test was not satisfied because there was no expectation of profits to be derived solely from efforts of others. The court stressed that this was an ordinary commercial loan transaction which Congress did not intend to regulate because it "would have no impact on the securities markets."

Steel based its argument on several decisions of courts within the Second Circuit which, despite Forman, have found securities to exist due to the literal language of the statutes. The Seventh Circuit correctly rejected this argument and looked through the form to the substance of the transaction, noting that

Steel's reliance on its lead lender, the Mortgage Company, for credit evaluations and day-to-day monitoring of the loan does not, as Steel argues, convert its loan participations into securities. Steel in fact conducted its own investigations of the project, and the extent of its

196. Id. § 78c(a)(10).
198. 635 F.2d at 1253.
200. 635 F.2d at 1253-54.
201. Id. at 1254.
202. Id.
203. Id. See cases cited id. at 1254 n.8.
control over management of the loan belies its suggestion that it was dependent on the Mortgage Company's entrepreneurial efforts in this venture.\textsuperscript{204}

In \textit{Frederiksen v. Poloway}\textsuperscript{205} the Seventh Circuit held that the purchaser of 100\% of the stock of a small corporation had not purchased a "security" for purposes of determining whether a violation of rule 10b-5 had occurred. The court found that the purchaser had taken control of the management of the corporation and therefore was not seeking to earn profits through the efforts of others.\textsuperscript{206} The plaintiff's strongest argument was that the definition of the term "security" includes "stock," which was in fact what the plaintiff had purchased. The Seventh Circuit had no trouble rejecting this argument on the basis of (1) \textit{Forman}, (2) the fact that the statute qualifies the definition of "security" with the language "unless the context otherwise requires," and (3) an old rule of statutory construction "'that a thing may be within the letter of the statute and yet not within the statute, because not within its spirit.'"\textsuperscript{207}

\textit{McGrath v. Zenith Radio Corp.}\textsuperscript{208} provided a much more difficult setting in which the court had to determine the definition of a "security" for purposes of liability under rule 10b-5. Robert McGrath was Vice-President and General Manager of H.R. Basford Co., of which he owned a modest number of shares of stock and options to purchase additional shares. Less than a year after he became an employee of Basford and acquired his stock, Zenith Radio Corporation, the major shareholder of Basford, decided to buy out the minority shareholders, all of whom were Basford employees. McGrath negotiated an agreement on behalf of Basford employees under which Zenith would pay $38 per share for the Basford stock. The fairness of the agreement was not an issue in the case.

Zenith argued that, under \textit{Frederiksen},\textsuperscript{209} the economic reality of the transaction was a sale of assets rather than a security since all of the minority stock was being sold at one time. The court rejected this, stating that

\begin{quote}
[t]o conclude otherwise would be to hold that a purchaser of corporate shares may deprive investors/sellers of the protections of the se-
\end{quote}

\textsuperscript{204} Id. at 1254.
\textsuperscript{205} 637 F.2d 1147 (7th Cir.), cert. denied, 451 U.S. 1017 (1981).
\textsuperscript{206} 637 F.2d at 1152.
\textsuperscript{207} Id. at 1150 (quoting Church of the Holy Trinity v. United States, 143 U.S. 457, 459 (1892)).
\textsuperscript{208} 651 F.2d 458 (7th Cir. 1981). The court discussed the issue in a long footnote. \textit{See id. at 467 n.5.}
\textsuperscript{209} \textit{See} notes 205-07 \textit{supra} and accompanying text.
curities laws if it can arrange that all of the corporation's shares are purchased at one time. Whatever the breadth of language, clearly Frederiksen does not require such a result.210

From the standpoint of Zenith, the transaction did not involve the purchase of a security since it was assuming complete control of the company. Nonetheless, the Seventh Circuit properly concluded that the transaction involved the sale of a security by the employees even if there was no acquisition of a security by Zenith that could have supported a Zenith claim under the SEC.

The "In Connection With" Requirement

The principal issue in McGrath was whether the deceptive conduct occurred "in connection with the purchase or sale of a security, as required by rule 10b-5."211 At the time McGrath was hired by Basford, he was told by President Amile Forni that he would succeed Forni when the latter retired. McGrath discussed his future with Walter Fisher, a Zenith executive, and was told that he, McGrath, was the "heir apparent" to Forni and that that was acceptable to Zenith. During this conversation, McGrath agreed to relinquish his option to buy Basford stock. Immediately after this meeting, Forni informed Fisher that he had serious doubts as to whether McGrath was a suitable successor. Forni and Fisher agreed that Forni would wait another three to four months before deciding. McGrath was not informed of this conversation and two days later sold his stock, along with other Basford employees, to Zenith and signed an agreement waiving his option rights. Several months later McGrath was fired.

The Seventh Circuit held that the failure of Fisher to disclose his conversation with Forni regarding his reservations about McGrath's future constituted a violation of rule 10b-5.212 This conclusion provided the federal jurisdictional basis for deciding pendent state claims of breach of contract and fraud.213 The district court jury awarded damages of $2,000,000. The Seventh Circuit found the jury's estimate of damages speculative and gave McGrath the option of accepting $1,300,000 or having a new trial on damages.214

The result provoked a sharp dissent by Judge Swygert. He argued

210. Id.
212. 651 F.2d at 467.
213. Id. at 463.
214. Id. at 474.
that McGrath could not have been induced to sell his stock or relinquish his option rights by the promise of the presidency because

[h]is right to keep his shares and the opportunity to buy more shares were contingent upon his continued employment by Basford. He could have been fired at any time. Under the terms of his contract, his right to buy more shares would have been extinguished [by his firing], and he could have been forced to sell . . . his acquired shares to the employee stock trust at less than book value.215

The majority rested its rule 10b-5 decision on McGrath’s sale of his shares and therefore found it “unnecessary” to address the question whether the waiver of the option rights also constituted a sale for purposes of rule 10b-5.216

The court found that the promise of the presidency was “in connection with” the sale of the stock because the “fraud may be said to ‘touch’ the transaction involving the purchase.”217 It is difficult to understand, however, exactly how the promise of the presidency touches the sale of the stock. The promise was made after the selling price of the stock was established and there was no suggestion that the $38 per share price paid was unfair. The essence of a rule 10b-5 violation is deception with regard to the value of what is being received or given up—in effect, deception with regard to the fairness of the transaction. There certainly was no deception regarding the amount of cash to be received in exchange for the stock. If the promise of the presidency is viewed as additional value given in exchange for the stock, then McGrath might arguably have been deceived with regard to the value of all he was to receive in exchange for his stock.

If the promise of the presidency was indeed consideration for the sale of the stock, a more serious problem is presented. McGrath negotiated the agreement with Zenith on behalf of Basford and its employees. He presumably recommended to the employees that they accept the $38 per share that they were being offered. If McGrath was being offered more than $38 per share for his stock, whether in cash or in the form of employment benefits, that fact would have to be disclosed to the Basford employees. Failure to do so would probably constitute a rule 10b-5 violation. In sum, if the majority truly believed that McGrath was receiving $38 per share plus the promise of the presidency in exchange for his Basford stock, then it is difficult to understand why

215. Id. at 475 (Swygert, J., dissenting).
216. Id. at 467.
217. Id.
they would reward his deceptive conduct with regard to the other employees by giving him $1,300,000.

Of course, it is possible to view the promise of the presidency as having been given in exchange for McGrath’s waiver of his option rights. The promise of the presidency was made by Fisher during the conversation in which McGrath agreed to waive the option. But Judge Swygert deals with this argument rather convincingly.218

Overall, it is difficult to understand why the court felt that McGrath had a claim under rule 10b-5 or even under state law. McGrath had been hired as the heir apparent but he could have been fired at will. If Fisher had told McGrath he was no longer heir apparent, McGrath would have had two choices: to sell his stock and waive his option or to refuse to sell or waive. Had he chosen the latter, he probably would have been fired. He then would have been required to sell his stock, his option rights would have automatically expired and he would have no rule 10b-5 claim. Zenith was, in effect, penalized $1,300,000 for giving McGrath another few months to prove himself. Rule 10b-5 does indeed still have a very broad range.

Statute of Limitations

Civil actions for damages under section 10(b) of the Securities Exchange Act of 1934219 are not expressly authorized by statute. However, the federal courts long ago recognized an implied right to bring such actions.220 Determining the appropriate limitation period for bringing such implied actions has caused considerable controversy. Federal courts have held that the limitation period should be that specified by the forum state statute that most closely resembles section 10(b).221 In most states there are three limitation periods that can be considered: (1) the securities law statute of limitations, (2) the common law fraud statute, or (3) the catch-all statute of limitations.222 A majority of circuits have opted for the first possibility223 and several circuits have opted for the second.224 No circuit has opted for the third possibility.225

218. See text accompanying note 221 infra.
222. See Cahill v. Ernst & Ernst, 625 F.2d 151, 152 (7th Cir. 1980).
223. See cases cited id. at 154 n.6.
224. See cases cited id. at 154 n.7.
225. See id. at 155.
In *Cahill v. Ernst & Ernst*, 226 a case before the court a second time,227 the Seventh Circuit had to decide the appropriate limitation period for a Wisconsin case under section 10(b). The Seventh Circuit had previously held that similar Illinois and Indiana cases were to be governed by the Illinois and Indiana securities law limitation periods, respectively.228 Unfortunately, the Wisconsin securities laws are not as clear as those of Indiana and Illinois. As a result the majority had to struggle to justify application of the Wisconsin securities law limitation period and Judge Pell, in dissent, argued for application of the catch-all limitation period.

Section 551.59 of the Wisconsin Statutes229 provides a cause of action against individuals who offer to sell securities in violation of the registration provisions of the Act or utilize deceptive or misleading methods. The limitation period for actions under section 59 is one to three years.230 Initially, the district court held that section 59 was the statute most closely resembling section 10(b).231 On appeal, the Seventh Circuit vacated the decision and remanded with instructions to consider whether section 551.41 of the Wisconsin Statutes232 more closely resembled section 10(b).233 On remand, the district court again decided that section 59 was the appropriate statute234 and the Seventh Circuit affirmed.235

The language of section 41 is virtually identical to that of rule 10b-5. Like rule 10b-5, no express remedy is provided for a violation. In its memorandum opinion vacating and remanding the district court's original decision, the Seventh Circuit asked the district court to consider whether there was an implied remedy under section 41.236 If there was, the district court was instructed to consider further whether the catch-all limitation period would apply under Wisconsin law and whether from a policy standpoint the federal courts should adopt such

226. 625 F.2d 151 (7th Cir. 1980).
227. For the procedural history of the case, see notes 237-42 infra and accompanying text.
228. See, e.g., LaRosa Bldg. Corp. v. Equitable Life Assurance Soc'y, 542 F.2d 990 (7th Cir. 1976) (court applied two-year statute of limitations from Indiana securities law); Parrent v. Midwest Rug Mills, Inc., 455 F.2d 123 (7th Cir. 1972) (court applied three-year statute of limitations from Illinois securities laws).
230. Id. § 551.59(5).
231. 448 F. Supp. 84, 86 (E.D. Wis. 1978).
233. 588 F.2d 835 (7th Cir. 1978).
235. 625 F.2d 151 (7th Cir. 1980).
236. 588 F.2d 835 (7th Cir. 1978).
a catch-all provision. On appeal the second time, the Seventh Circuit majority accepted the district court’s determination on remand that the legislative history of section 41 suggested no intent to provide an implied remedy, that sections 41 and 59 were aimed at prohibiting the same kinds of conduct and that it would be anomalous to have different limitation periods for the two statutes.237

Judge Pell, in dissent, argued that, although sections 41 and 59 were aimed at the same conduct, section 59 was not intended to cover the same conduct as rule 10b-5, but instead was analogous to section 12 of the Securities Act of 1933.238 Among the other important differences he noted between sections 41 and 59 were: (1) section 41 imposes liability on “any person” while section 59 imposes liability only on parties who sell or offer to sell securities, control persons, broker-dealers and their agents; (2) section 59 limits the damages recoverable while section 41 has no such provision; and (3) section 59 allows recovery for damages resulting from negligent conduct while section 41 provides no such relief.239

After concluding that sections 41 and 59 are different, Judge Pell argued that there is an implied right of action under section 41. The Wisconsin securities laws are based on the Uniform Securities Act with some modification. However, Wisconsin deleted from section 59 of the uniform act the phrase “but this act does not create any cause of action not specified in this section.”240 This deletion, for Judge Pell, was a conclusive indication of legislative intent.241 His conclusion was strengthened by the fact that the Cahill defendants were accountants who could not be subject to liability under section 59 because they did not sell any securities. He stated,

[I]t is not reasonable to believe that the legislature did not intend to grant people such as the present plaintiff a private right of action. Because it appears to me beyond question that [section 41] does provide for a private cause of action, and that plaintiff should have been permitted to proceed under that section, the only statute of limitations which can have applicability is the catch-all six year provision.242

This case is another in a long series that has struggled with limita-

237. 625 F.2d at 155.
239. 625 F.2d at 157.
240. Id.
241. Id.
242. Id.
tion period problems under section 10(b) and rule 10b-5. The amount of public funds expended by the judicial system and the private funds expended by litigants in contesting statute of limitations problems must be substantial. These costs are one reason for the courts to be particularly cautious in implying remedies. On the other hand, it is surprising that there has been no legislation to clarify this matter. The proposed Federal Securities Code, if enacted, will solve the problem. It provides for a one- to five-year limitation period.

In *J.H. Cohn & Co. v. American Appraisal Associates, Inc.*, the Seventh Circuit was faced with a procedural issue involving statutes of limitations: whether waiver of the right to assert the statute of limitations as a defense was binding in a subsequent case between the same parties. This case illustrates once more the amount of time and money that is wasted because of the lack of a uniform statute of limitations. The case was brought as a class action in federal district court in New York, which applies a six-year limitation period under New York law, and then transferred to the federal district court in Wisconsin which, on the basis of Cahill, applies a three-year limitation period. Some of the plaintiffs would have been barred from asserting claims by application of a three-year limitation period but not by application of a six-year period.

As a condition of transfer the United States District Court for the Southern District of New York exacted a promise that "no defendant will raise a statute of limitations defense in the Eastern District of Wisconsin." At the time of the transfer, the court had not certified the class. The Wisconsin court subsequently refused to certify the class and sixty-four members of the class that sought to be certified filed individual actions.

The Seventh Circuit held that the defendants were estopped from asserting the statute of limitations as a defense because of the New York agreement, despite the fact that they were technically entitled to such an assertion. They had not waived their rights against the individual plaintiffs because the individual plaintiffs had not filed their

244. All Fed. Sec. Code § 1727(b) (Mar. 1978 Draft).
245. 628 F.2d 994 (7th Cir. 1980).
247. 628 F.2d at 1000.
248. Id.
249. Id.
complaints (which were virtually identical to the class complaint) in the Southern District of New York. Had the plaintiffs so filed, they clearly would have been protected under the New York agreement. However, the court found that the plaintiffs had been misled as to the effect of the agreement because it was ambiguous.250 Therefore, on equitable grounds, the court held that the defendants were estopped from asserting the statute of limitations as a defense.251

Vicarious Liability

A broker-dealer who fails to properly supervise an employee can be held liable under section 20(a) of the Securities Exchange Act of 1934252 for losses to customers caused by the employee’s actions. In Henricksen v. Henricksen,253 the plaintiff, Wendee Henricksen, sought damages from her former husband, George, and his broker-dealer employer, Smith Barney, Harris, Upham & Co. The claim was based on conversion of $55,356, trading losses of $33,564 in purchases of calls and $21,754 in commission charges and margin interest.

There was no question about George’s liability for converting funds. He was also held liable for the other losses because he exercised his discretionary authority to make trades in a manner inconsistent with Wendee’s stated investment goal.254 Liability was predicated on both state common law255 and section 10(b) of the Securities Exchange Act of 1934.256 The section 10(b) liability was based on the court’s finding that the entire pattern of activity constituted a scheme to defraud.257

The district court found Smith Barney liable for the $21,754 of commissions and interest on a common law theory of unjust enrichment, but declined to hold the firm liable for the other amounts.258 The court held that Smith Barney was "entitled to rely on George’s investment decisions because Wendee had given him broad discretionary power over the accounts."259 The Seventh Circuit correctly found this to be a misperception of the legal relationships. George was not

250. Id.
251. Id. at 1001.
253. 640 F.2d 880 (7th Cir. 1981).
254. Id. at 884.
255. Id. at 887.
256. Id. at 884.
257. Id.
258. Id.
259. Id. at 886.
Wendee's agent; rather, "Wendee's agent in the management of her accounts was Smith Barney as represented by their agent George Henricksen." The Seventh Circuit found Smith Barney's common law liability to be clear and reiterated its statement from a prior case that "[u]nder common law principles, a principal is liable for the deceit of its agent committed in the very business he was appointed to carry out. This is true even though the latter's specific conduct was carried on without knowledge of the principal."  

Liability was also based on section 20(a) of the Securities Exchange Act of 1934, which imposes liability on persons in control of anyone held liable under the Act. It is a defense under section 20(a) if "the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action." The court in effect held that Smith Barney's conduct had at least indirectly induced the acts because Smith Barney had failed to follow its own internal rules for handling discretionary accounts. Specifically, (1) seventeen out of forty trades in Wendee's account were not approved by the branch manager, despite a requirement that they be so approved; (2) purchases of calls were made even though the account was not approved for such speculative activity; and (3) Wendee's account was not reviewed for excessive activity during several months when it should have been. 

Smith Barney argued that because George and Wendee were husband and wife it was relieved of supervisory responsibility. The court held that, if anything, this relationship increased Smith Barney's duty. But for the marital relationship between George and Wendee, this would have been a routine case for imposition of liability under section 20(a).

INSIDER TRADING

Section 16(b) of the Securities Exchange Act of 1934 imposes liability on corporate insiders for any profit derived from the purchase and sale of their corporation's securities within a six-month period. The purpose of section 16(b) is to "protect the 'outside' stockholders

260. Id
261. Id at 887 (quoting Fey v. Walston, 493 F.2d 1036, 1052 n.19 (7th Cir. 1974)).
263. Id
264. 640 F.2d at 885-86.
265. Id at 887.
against at least short-swing speculation by insiders with advance information."  

The Seventh Circuit had two section 16(b) cases this past year, both concerned with the definition of a "sale." In *Portnoy v. Revlon, Inc.*, the issue was one of timing—when the sale actually occurred in a corporate merger. In the other, *Oliff v. Exchange International Corp.*, the issue was whether a sale ordered by a probate court was a sale within the meaning of section 16(b).

*Portnoy v. Revlon, Inc.* was a derivative suit brought on behalf of Revlon, Inc. against Cooper Laboratories, Inc. The suit was brought in the aftermath of a modest fight for control of Barnes-Hind Pharmaceuticals, Inc. Cooper steadily purchased B-H shares beginning in 1972 and, as of February 27, 1976, it owned more than 10% of B-H, thus making it an insider for purposes of section 16(b). In May 1976, Cooper bought an additional 88,000 shares of B-H for $4,253,282. B-H decided to resist Cooper's creeping acquisition attempt and arranged a merger with Syntex Corporation. Cooper opposed this arrangement but agreed to support an alternative proposal for a B-H merger with Revlon.

On June 11, 1976, B-H and Revlon signed a letter of intent to merge. On July 29, B-H and Revlon signed a merger agreement, pursuant to which the closing and exchange of shares occurred on December 31. Cooper made a profit of $1,555,000 on the shares it had purchased in May. The district court held that the sale occurred on December 31, more than six months after Cooper's May purchase, and therefore there was no section 16(b) liability.

On appeal, the plaintiff argued that the sale occurred on either June 11 or July 29, the dates of the execution of the letter of intent and the merger agreement, respectively. The court had little trouble dismissing the June 11 date since the letter of intent was not a binding agreement and Cooper explicitly retained its right to sell its shares to others. The July 29 agreement required more analysis. The court was faced with the Ninth Circuit's holding in *Provident Securities Co. v.*

269. 650 F.2d 895 (7th Cir. 1981).
270. [1980] FED. SEC. L. REP. (CCH) ¶ 97,634 (7th Cir. Sept. 18, 1980).
271. 650 F.2d 895 (7th Cir. 1981).
272. Hereinafter referred to as B-H.
273. 650 F.2d at 897.
274. Id. at 899.
Foremost-McKesson, Inc.\textsuperscript{275} that the date an underwriting agreement was signed, and not the closing date, was the date of sale.\textsuperscript{276}

The court distinguished \textit{Portnoy} from \textit{ Provident Securities} on its facts. \textit{Portnoy} did not involve an underwriting; furthermore, the \textit{Portnoy} merger agreement had a number of significant conditions precedent to closing. Those included: (1) an IRS ruling that the merger would be tax exempt (this ruling was received on December 7, 1976); (2) an accountant's opinion that the merger would qualify for "pooling of interest" accounting; (3) exercise of dissenting shareholder appraisal rights by less than 27,380 shares (these rights were exercisable until December 30, 1976); (4) execution of employment agreements by certain B-H employees; and (5) execution of noncompetition agreements by certain B-H shareholders.\textsuperscript{277}

\textit{ Provident Securities} did not involve an agreement with conditions like those in \textit{Portnoy}. Indeed, the only significant condition that had to be satisfied in \textit{ Provident Securities}, that a registration statement become effective, was satisfied on the date the agreement was signed. The Seventh Circuit found the required IRS ruling and dissenters' rights conditions particularly significant.\textsuperscript{278} However, experienced tax counsel and financial advisers are not likely to allow their clients to enter into such agreements unless they know on the basis of experience that conditions like these are virtually certain to be satisfied.

The \textit{Portnoy} result nonetheless is correct, even though alternative grounds to support the holding may have been stronger.\textsuperscript{279} Cooper was not an insider from whom the market needed protection from speculative abuse. Cooper was a hostile threat to B-H management—it was not part of management.

In \textit{ Oliff v. Exchange International Corp.},\textsuperscript{280} the court affirmed a decision imposing liability under section 16(b) on the estate of George Sax. On December 22, 1975, the estate purchased 14,318 shares of Exchange International Corporation for $10.49 per share from the Sax Foundation. The purchase was made in order to relieve the estate of

\textsuperscript{275} 506 F.2d 601 (9th Cir. 1974), \textit{aff'd on other grounds}, 423 U.S. 232 (1976).
\textsuperscript{276} 506 F.2d at 614.
\textsuperscript{277} 650 F.2d at 900.
\textsuperscript{278} \textit{Id.} at 900 n.6.
\textsuperscript{279} The district court in \textit{Portnoy} held that Cooper's exchange of stock was exempt from § 16(b) under Kern County Land Co. v. Occidental Petroleum Corp., 411 U.S. 582 (1973). 650 F.2d at 897. The two cases are strikingly similar although Cooper's sale was probably not as involuntary as Occidental's. For additional theories supporting Cooper's position, see \textit{Id.} at 897 n.4.
\textsuperscript{280} [1980] \textit{FED. SEC. L. REP. (CCH)} \textsection 97,634 (7th Cir. Sept. 18, 1980).
any potential tax liability for alleged self-dealing by George Sax with the foundation during his lifetime. On May 7, 1976, pursuant to a probate court order, the estate sold 190,727 shares for $18.59 per share.

The estate owned more than 10% of Exchange on December 22, 1975, the date of purchase, and on May 7, 1976, the date of sale. Since the transaction resulted in a profit within six months, there was clearly technical liability under section 16(b). The real issue was whether the court would be willing to relieve the estate of liability under the “pragmatic” approach of the Supreme Court in *Kern County Land Co. v. Occidental Petroleum Corp.* To be relieved of technical liability under *Kern County*, (1) the purchase or sale must be an unorthodox transaction, and (2) an analysis of the transaction must disclose no possibility of short-term speculative abuse. The court refused to relieve the estate of liability because it did not satisfy this two-step analysis.

The court did not find anything unorthodox about the sale. The sale was not compelled by the probate court; the probate court had simply set up orderly procedures to determine the buyer since the three executors disagreed as to who should be permitted to buy the stock. Since the court viewed the sale as being voluntary and also thought that there was potential for abuse—the three executors were all Exchange insiders—it had no trouble imposing section 16(b) liability on the estate.

The result is questionable. The estate owned 176,409 shares of Exchange. In order to avoid a tax assessment of $307,000 it purchased an additional 14,318 shares. In spirit at least, this appears to have been an involuntary purchase. It was made at virtually the same time that the estate decided to sell its Exchange stock. Because of a dispute among the trustees, the sale was finally made through a court-arranged auction. The combination of a tax-induced “involuntary” purchase and a court-ordered sale seems to satisfy the “unorthodox transaction” test required by *Kern County*. Similarly, it is hard to believe that an involuntary purchase at a time when active efforts to sell are underway involves the likelihood of speculative abuse. It appears that the court focused too much on the estate’s potential access to inside information.

284. *Id.*
and not enough on the serious dispute among the estate’s executors. The dispute appears to satisfy the Kern County requirement that the transaction involve no possibility of short-term speculative abuse.

CONCLUSION

The most important case of the term was Panter v. Marshall Field & Co.285 It is noteworthy because of the economic importance of tender offers and the uncertainty regarding the duties of the target corporation’s board of directors. The most significant aspect of the case involved a state law issue—whether the business judgment rule applies to directors’ actions when faced with a hostile tender offer. While many are likely to be unhappy with the court’s decision, it is not surprising that the court was reluctant to act boldly in an essentially uncharted area of state law. The other decisions this term were generally well-reasoned opinions adding texture but not new patterns to the federal securities law.

285. 646 F.2d 271 (7th Cir. 1981). See notes 19-94 supra and accompanying text. The Marshall Field saga continues. As this issue went to press, Field’s was once again in the midst of a takeover attempt. In early 1982, an investment group headed by Carl C. Icahn acquired approximately 30% of Field’s stock at an average price of about $19 per share. The Field’s directors, in an effort to fend off Icahn, agreed to a buyout by Batus Inc., a British company. The buyout price was $25.50—far below the $42 per share proposed offer from Carter Hawley Hale four years earlier. Several days after the Field’s board agreed to the $25.50 price, Batus increased its offer to $30 per share. The bidding for Field’s may well go over $30 but is not likely to reach the $42 CHH proposed offering price. Even if it did, the Field’s shareholders would still have been financially better off with the CHH offer. After four years, assuming a 10% earnings rate, $42 would have grown to about $61.50.

It is clear that the passage of time has not vindicated the Field’s directors’ decision to reject the CHH offer. To the extent that there might have been legitimate antitrust concerns regarding a CHH takeover, there would appear to be similar concerns regarding Batus. Batus owns Saks Fifth Avenue, which operates 32 specialty stores nationwide including 2 in the Chicago area; Gimbel Bros., which operates 38 department stores nationwide; Thimbles Specialty Fashion Stores, a discount department store with 8 units in as many states; and Kohl’s Supermarkets and Department Stores with 17 stores in Wisconsin and Illinois. It is difficult to believe that a CHH acquisition raised more antitrust issues than a Batus acquisition.

The best that can be said on behalf of the Field’s board is that in 1977 they believed it important to retain local control of a major local institution and that they believed that there was a reasonable chance that they could increase the value of Field’s stock beyond $42. It is certainly clear now, if it was not then, that they were excessively optimistic.