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March 1, 1983

Linda C. Quinn
Associate Director
Corporation Finance Division
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Re: Advisory Committee on Tender Offers

Dear Ms. Quinn:

I have reviewed the documents and outline I received the other day and have only a few thoughts to pass on.

As I'm sure you know, I have published my views on tender offers. The articles set out my general approach and ideas on both the role of tender offers and the consequences of regulation. There is little point in rehearsing them here. I enclose one recent piece, with Dan Fischel, entitled Corporate Control Transactions, describing the structure of my approach. I also enclose the page proofs of a piece, forthcoming in the next issue of the Stanford Law Review, describing my position on defensive tactics and tender offer auctions.

In brief: the first-best world for investors (in bidders and targets alike; or in both, as most investors have diversified portfolios) is one on which there is no Williams Act but there is a strictly-enforced prohibition of fraud; the second-best world is one in which the Commission implements the Williams Act according to its terms and does not extend any of the statutory periods of time, and in which state law inhibits defensive tactics by targets; and any other world is a distant third. As we live in such a distant third-best world, I think the attention of the Advisory Committee should be devoted to addressing how to get from here to a second-best world.

These views have a direct application at almost every point in the outline. I'll spare you a rundown.

I am concerned, however, that the outline is too comprehensive. A group of 16 diverse people as diverse as this one will find it impossible to discuss, let alone to agree on, even a small set of the issues noted in the outline. I would prefer to see the list of topics greatly pared down. A leaner agenda would

pose for the Committee a series of fundamental questions: first, what do we know about the consequences of tender offers for investors' welfare; second, what do we know about the consequences of existing (or potential) regulation for the number of offers; third, should regulation be designed to maximize the welfare of investors taken as a group (that is, as people who can and do hold positions in both bidders and targets) or only the investors who happen to hold positions in targets? The third issue, in other words, is: do we look at regulation (and its consequences) ex ante, when investors are ignorant of which firm will seek to acquire which other firm and are interested only in maximum total returns, or do we look at regulation ex post, once a bid is on the table? The ex post approach downplays the effects of regulations on the number of offers and emphasizes questions concerning how to maximize the price paid and to spread the gains equitably. The ex ante approach requires close attention to effects on the number of offers and in turn downplays concerns about "equal treatment," because ex ante all investors are treated equally automatically to the extent the prices they pay depend on information about the likelihood of offers. It also entails little concern about higher prices, because potentially-diversified investors lose as holders of bidders what they gain as holders of targets and therefore care about all beneficial offers going foreward rather than about the allocation of gains. These and other questions are addressed in the two articles I have enclosed.

I think the Committee shall not be able to make much headway unless it tackles these basic issues first. And if it tackles and reaches consensus on them, then the solutions to many of the practical problems of regulation follow rather quickly. Without consensus, though, debate on particular problems will continually degenerate, as members revive unsettled questions going back to first principles. Thus my fundamental suggestion thus is that the Committee's initial work be organized along the lines laid out above.

Such an organization means that the Committee would depend on the staff for substantial aid. The materials you sent to the members of the Committee were long on the sort of things usually found in the financial press and the law journals, short on the insights of economic analysis of law and financial economics. I think it is essential to bring to bear the economic approach to financial and legal matters. Thus one important task would be to provide to members of the Committee with knowledge of what this literature establishes.

Perhaps the staff could provide such knowledge either by rounding up and making a precis of each articles or by producing an essay after the fashion of the Journal of Economic Literature that summarizes what we <u>know</u> about tender offers. Much of what we know is contained or cited in the papers forthcoming in volume 11 of the Journal of Economic Literature. If the staff does not already have these papers, I'm sure that the Editor of the JFE,

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Michael Jensen at Rochester's Graduate School of Management, would furnish them. Greg Jarrell, one of the members of the Committee, has been a contributor to this literature and could suggest appropriate starting points (and also furnish you with his latest empirical papers). My published work on tender offers also contains some brief summaries. The survey essay usefully could be organized by looking first at the institution of tender offers and then at each step in an offer and defense, asking, for each, who gains and how much.

I would be happy to expand on these remarks by phone. You may reach me at (312) 753-2440 or (312) 580-0243.

I look foreward to meeting you and beginning the Committee's work on March 18.

Sincerely,

Frank H. Easterbrook

Frank H. Easterbrook
Professor of Law