509403
1110
BE001
BE003
FG006-11
FG249

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

MEMORANDUM FOR HOWARD BAKER

THROUGH: James C. Miller III

FROM: Joseph R. Wright, Jr.

WRS

SUBJECT: Dingell-Markey Tender Offer Reform Act of 1987

On Monday, Congressman Dingell and Markey introduced the "Tender Offer Reform Act of 1987." While numerous legislative proposals to restrict corporate takeover activity have been introduced this year, none have been reported out of committee. The Dingell-Markey bill, however, is likely to be reported out.

The basic goal of the Dingell-Markey bill is "to restore stability to our financial markets by curbing abusive and unfair tactics employed by both raiders and management," and it focuses on the tender offer process. Its major provisions include:

- Closing the "13d Window." Currently acquirers of 5% or more of a firm's stock must report the acquisition to the Securities and Exchange Commission (SEC) and the issuer within 10 business days. Dingell-Markey would shorten the reporting period to 24 hours and forbid further purchases for two days after the notice is filed.

- Requiring the acquisition of 10% or more of a firm's stock to be made by tender offer.

- Establishing a 60-calendar day minimum tender offer period instead of the current 20-business day minimum.

- Requiring the one-share, one-vote standard for publicly traded corporations. Currently, sixteen firms traded on the New York Stock Exchange have dual classes of common stock with disparate voting rights. In recent years, seventeen firms on the American Stock Exchange and twenty-six firms traded over the counter have issued dual classes of stock.

- Prohibiting "Golden Parachutes." These guarantee substantial severance payments to top management if they lose their jobs as a result of a takeover.

- Prohibiting "Greenmail." Greenmail occurs when a company purchases its own stock from a raider at a premium to prevent a hostile takeover. Dingell-Markey would restrict such actions if 3 percent or more of the stock has been

held by a raider for less than 2 years, unless shareholders approve or if the same price is offered to all shareholders.

- o Authorizing the SEC to develop restrictions for other defensive tactics such as "poison pills" and "tin parachutes."

- o Banning market sweeps and similar purchases outside the Williams Act.

The Dingell-Markey Bill amends and substantially increases the scope of the Williams Act, the Federal law that governs tender offers. The Bill would make all takeovers, including hostile ones, more difficult and more expensive by increasing the Federal regulation of bidders. The Bill also extends Federal regulations in areas not heretofore covered by the Federal government -- those governing defensive tactics and one-share, one-vote.

The Williams Act now governs only the disclosures that must be made in a tender offer, the minimum time periods that must be observed by the parties, and the rights of tendering shareholders. The Williams Act does not address either the merits of any particular offer or type of offer, nor does it make any attempt to deal with the question of defensive tactics. The Williams Act leaves to the States the role of regulating the relationships between shareholders, managers, and prospective shareholders during a tender offer whether friendly or hostile.

Administration Position

The Administration's guiding principles with respect to takeover issues have been:

- o Strong enforcement against insider trading is a separate issue from regulatory takeovers.

- o States have and should continue their important role in corporate governance issues.

- o The SEC has done an excellent job in finding and remedying abuses.

Since 1985, the Administration's position on tender offer issues, with the exception of the "one-share, one vote" issue, has been to oppose any increased Federal intervention in the tender offer process (see attached). Generally, our position is that corporate governance is best controlled through State law and that the Federal government should become involved only as a last resort.

With regard to one-share one-vote, the SEC recently reviewed the New York Stock Exchange's request for Federal regulation. The Department of Justice filed with SEC its view that such Federal

regulation of shareholder's rights is unneccessary, and that shareholders are adequately protected by State law. The SEC has taken no action thus far. However, the Administration has not yet taken an official position.

We also, at this time, have no position on the "13d window". We need to examine this issue in light of the Supreme Court's recent decision on April 21 regarding the case of CTS Corporation vs. General Dynamics. The Court upheld the constitutionality of the State of Indiana's strict requirements for allowing shareholder approval or disapproval of management takeovers.

The Economic Policy Council (EPC) Working Group on Financial Transactions has considered addressing public concerns through: (1) vigorous law enforcement against securities industry wrongdoing; (2) an increase in the SEC's budget; (3) tough penalties against wrongdoers; and (4) evaluation of proposals to further develop the Administration's position.

Senate Action

So far, little movement has occurred in the Senate on corporate takeovers, but this could change in response to the House activity. We would expect Senator Proxmire, Chairman of the Senate Banking Committee, at a minimum, to reintroduce his bills of last session. These bills would:

- Require the approval of any acquisition by two-thirds of shareholders or a majority of the independent directors;
- Require the acquirer to evaluate the economic impact of the takeover; and
- Prohibit investments in "junk bonds" by any Federally insured depository institution.

Senator Proxmire has indicated that he may support proposals that would eliminate "greenmail" and slow the tender offer process.

Other Corporate Securities Issues

The public debate surrounding corporate takeovers involves several related issues, in addition to tender offers. These include:

- Insider Trading -- OMB is developing a definition of insider trading for consideration by the EPC Working Group on Financial Transactions.
- Corporate Debt Structure -- Over the past few years debt/equity ratios for corporations have increased substantially. Congress questions the need for such increases and has proposed legislation to restrict debt growth through the use of junk bonds and other creative

financing schemes.

- o Depository Institutions -- High yield securities (junk bonds) have been a major source of financing for hostile takeovers. Congress has questioned the appropriateness of allowing federally insured institutions to invest in such risky securities. The Administration has opposed additional restrictions on the investment in junk bonds by federally insured institutions.

- o Antitrust Issues -- Congress has proposed to deter mergers in general hostile takeovers. The Administration opposed legislative proposals to amend the Hart-Scott-Rodino pre-merger notification.

Next Steps

We should continue to separate the issues in order to keep the debate manageable and subject to rational analysis. In particular, the insider trading issue should be kept separate from the tender offer issues.

The SEC has done a good job in dealing with the insider trading scandals. No doubt, new revelations will keep the issue visible. In addition, the SEC, through its regular rule making process, has considered a number of the issues related to the Williams Act, and is in a good position to handle these questions and provide leadership in the future.

There are several alternative approaches we can take:

- o Hold to or modify previous positions on corporate takeovers, antitrust laws (merger policy), and junk bonds.

- o Develop positions on issues not yet addressed such as insider trading and corporate debt.

- o Work with interested members of Congress and outside groups to defend the Administration's position.

c: Duberstein
Ball
Cribb
Risque