LIPTON AND ROWE'S APOLOGIA FOR DELAWARE: A SHORT REPLY

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ABSTRACT

Three themes animate Martin Lipton and Paul Rowe's thoughtful response to my critical evaluation of Unocal's fifteen-year history. First, they maintain that affording shareholders a primary role in the governance of takeovers depends on a commitment to the stock market's informational efficiency. Second, they claim that allowing shareholders to amend or repeal a poison pill ignores empirical evidence that the existence of a poison pill is associated with higher takeover premiums. Third, they assert that the Delaware General Corporation Law (DGCL) reflects an implicit mega-principle that assigns control over takeovers to managers. This short reply corrects Lipton and Rowe's misunderstanding of the importance of market efficiency in assessing the efficiency of a primary role for shareholders in takeover decision making; suggests that the impact of a poison pill on takeover premiums depends entirely on what a court will allow a target company to do with its pill; and, finally, complicates Lipton and Rowe's argument that the structure of the DGCL implies a primary takeover role for the board.

I am flattered that Martin Lipton and Paul Rowe have written a lengthy and thoughtful response¹ to my reprise of the fifteen-year history of Unocal Corp. v. Mesa Petroleum Co.² Martin Lipton has a strong claim to having devised the most important innovation in corporate law since Samuel Dodd invented the trust for John D. Rockefeller and Standard Oil in 1879.³ Paul Rowe is an active and experienced practitioner who has also contributed to the debate over Delaware takeover law. Thus, if nothing

¹Charles J. Meyers Professor of Law and Business, Stanford University, and Marc and Eva Stern Professor of Law and Business, Columbia University. I appreciate the editors of the Delaware Journal of Corporate Law giving me the opportunity to offer this reply. I am also grateful to William T. Allen, Jeffrey Gordon, Michael Klausner, and Elliot Weiss for helpful comments on an earlier version.

²Martin Lipton & Paul K. Rowe, Pills, Polls and Professors: A Reply to Professor Gilson, 27 DEL. J. CORP. L. 1 (2002).

³Ronald J. Gilson, Unocal Fifteen Years Later (And What We Can Do About It), 26 DEL. J. CORP. L. 491 (2001); Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985).

else, it is an enormous, if perhaps somewhat backhanded, compliment that they thought my essay had sufficient potential for influence to warrant their substantial effort to challenge it.

To set the stage for purposes of this short reply, my essay offered a respectful, but in the end negative, assessment of the Delaware Supreme Court's post-
Unocal effort to walk a middle road between managerialists, like Mr. Lipton, who thought defensive tactics in tender offers were properly reviewed under the business judgment rule, and those, mainly academics, who thought that the ultimate decision concerning a tender offer belonged to the shareholders. This middle road—the Unocal intermediate standard—contemplated a regulatory role for the courts in that they themselves would determine whether a particular defensive tactic was reasonable in relation to the threat, if any, posed by the offer. In "Unocal Fifteen Years Later," I argued that the supreme court's subsequent development of the intermediate standard, culminating in Unitrin, has devolved into an unexplained preference that control contests be resolved through an election rather than the market. Unless a successful proxy fight by the bidder to remove the incumbent board "would either be mathematically impossible or realistically unattainable," it appears that the board may decline to redeem a poison pill, thereby preventing shareholders from having the opportunity to accept a tender offer. I suggested that the court's path was set by a well meant, but, with the benefit of hindsight, plainly incorrect concern that the hostile takeovers represented a macroeconomic threat, and that, correctly in this respect, only the Delaware courts were in a position to act.

Fifteen years of experience, as exemplified by Unitrin's unexplained electoral bias, counsels in favor of repositioning Delaware takeover law for the future. To that end, I offered a modest proposal. I did not suggest overturning Moran v. Household International, Inc.'s validation of a board's power to adopt a poison pill, nor did I suggest that the Delaware Supreme Court recant its post-Unocal doctrine. Rather, I recommended only that shareholders be allowed to amend or repeal an existing poison pill by adopting a bylaw to that effect.

Lipton and Rowe rather exaggerate the impact of this proposal. "If stockholders can tell the board that directors' fiduciary duties do not allow

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4 The tone of my response will reflect that compliment and largely (but not completely) ignore the hyperbole that from time to time appears in the Lipton & Rowe essay.


6 Id. at 1388-89.

7 500 A.2d 1346 (Del. 1985).
for adoption of a pill," Lipton and Rowe inform us, "then there are no teachings left of Unocal, Household, and Quickturn [Design Systems, Inc. v. Shapiro]." For better or worse, however, sanctioning a shareholder-adopted bylaw to amend or redeem a pill hardly puts Humpty Dumpty back together again. Repealing Household International would require the board to secure shareholder approval before adopting a pill. My modest proposal leaves board adopted pills (and the supreme court's unfortunate post-Unocal jurisprudence) in place, except in those circumstances when shareholders overcome the substantial costs of defeating management in a proxy contest over adopting the redeeming bylaw. This hardly merits Lipton and Rowe's characterization of it as the "wholesale rejection of the framework of Delaware law regarding takeovers."

But whether my proposal is modest or downright subversive, Lipton and Rowe certainly offer a different view of the doctrinal history, and a rather different assessment of the role of takeovers in corporate governance. Quite plainly, they have sought to offer the reasoned analysis of how the Delaware Supreme Court got to its holding in Unitrin that the court has not itself provided. Readers can assess our competing accounts of Delaware takeover doctrine without further assistance from any of the authors.

What does warrant further comment, however, are three themes that animate Lipton and Rowe's argument. The first is that affording shareholders a primary role in the governance of takeovers depends on an unequivocal commitment to the stock market's informational efficiency. The second is that allowing shareholders to repeal a poison pill ignores empirical evidence showing that the adoption of a pill increases takeover premiums. The third is that the Delaware General Corporation Law (DGCL), although silent with respect to target directors' power to block offers not directed to them, nonetheless incorporates an unstated meta-principle that privileges directors over shareholders with respect to all forms of takeovers. Part I of this reply addresses Lipton and Rowe's misunderstanding of the importance of market efficiency in assessing the shareholders' role in the governance of takeovers. Part II takes up the poison pill issue, suggesting that the pill is itself an empty vessel whose impact, transactionally and on share prices, depends on what standard governs its redemption. Finally, Part III complicates Lipton and Rowe's

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4Lipton & Rowe, supra note 1, at 3 (adding citation—Quickturn Design Sys. v. Shapiro, 721 A.2d 1281 (Del. 1998)).

5Id. at 2.
neat construction of the DGCL as reflecting an unstated meta-principle that allocates control over takeovers to management.

I. MARKET EFFICIENCY AND THE CORPORATE GOVERNANCE OF TAKEOVERS

The most puzzling aspect of Lipton and Rowe's criticism of my assessment of Delaware takeover law is their sharp focus on market efficiency. This concept, in their view, seems to separate the forces of darkness and light: "[o]n the one side are the partisans of the efficient market theory. . . . On the other side are a variety of other participants in the debate who do not accept the efficient market theory as the only, or the best, guide for corporate law decision making." Lipton and Rowe then complete their syllogism by arguing that efficient market theory has been discredited of late and, therefore, so too has the position of those who view shareholders as the ultimate decision makers in tender offers. The problem with this neat two-step is that it misstates the role of market efficiency in the analysis and also misstates or misunderstands the impact of recent criticism of market efficiency on the corporate governance role of takeovers.

The role of takeovers in corporate governance is by now a familiar story. Some forms of corporate underperformance may prove difficult to remedy internally. The product market often does not act with sufficient speed or intensity to police poor strategy or implementation. As well, the need for industry-wide restructuring—as, for example with the failure of the conglomerate experiment—may be difficult to perceive from within the industry and the corporation. Under these circumstances, traditional legal rules are ill suited to resolve concerns about these kinds of underperformance. Courts cannot distinguish with precision whether underperformance results from bad luck on the one hand, or bad judgment on the other. The business judgment rule properly serves to allocate that assessment to the market. If underperformance persists, the value gap may come to exceed the costs of mounting a hostile tender offer. The issue of defensive tactics arises in this context. Target management's efforts to block a takeover may reflect a good faith effort to secure a better price for

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10 Id. at 2-3. Elsewhere, Lipton and Rowe identify "the primacy of the outcomes defined as optimal by the efficient market theory" as one of the "false premises" underlying my theses. Id. at 19.

11 This analysis is developed in Ronald J. Gilson, A Structural Approach to Corporations: The Case Against Defensive Tactics in Tender Offers, 33 STAN. L. REV. 819 (1981).
shareholders, or it may reflect entrenchment—a preference of target management to maintain the status quo.

So far, we only have an agency problem. Market efficiency now comes into play in two different ways. First, one might take the position that the target company's current market price is a sufficiently good measure of the company's value that even a very small premium is an advantage to target shareholders. In this view, advanced originally by Judge (then Professor) Frank Easterbrook and Professor Daniel Fischel, one could argue that target management should be entirely passive in the face of a hostile tender offer, fore-going even an effort to secure a better price. From the perspective of target company shareholders, this argument places significant reliance on the target company's stock price as an accurate measure of value because the attractiveness of a small premium is sensitive to small differences in underlying value.

The other position is that target management should be permitted to deploy defensive tactics to provide sufficient time to secure a better offer or to persuade shareholders that remaining independent would result in greater long-term value. This position recognizes that share prices may not reflect information about the company known only within the corporation, and that target management can enhance the corporation's share price by disclosing that information. It further recognizes that management can use delay to negotiate a higher price for shareholders or to attract a competing bid. In the end, however, shareholders decide whether to accept the offer. This position is significantly less dependent on the relative degree of market efficiency, because the process of seeking an alternative offer and informing shareholders of previously private information will improve the market's pricing. I should also note a point to which I will return shortly. This position is not inconsistent with Mr. Lipton's poison pill. Indeed, the

14Lipton and Rowe complain about the labeling of Lipton's innovation with the term
pill is an effective way of securing sufficient time for management to seek out an alternative bid or communicate with shareholders. The position is only inconsistent with Mr. Lipton's preferred construction of the pill—that the pill allows blocking the shareholders from ever having the opportunity to accept the offer.

This is the point where agency theory and market efficiency intersect. Management may have nonpublic information concerning the value of the corporation that convinces them that the tender offer price is too low. Nothing in efficient market theory is inconsistent with this circumstance. The shareholder choice position does not depend on the stock market being strong form efficient, i.e., that share prices reflect information that only management knows.

That leaves us with a balance. On the one hand, as Lipton and Rowe want to emphasize, management may know something that the market does not. On the other, as they are inclined to ignore, management may be resisting the tender offer out of either self-interest or error. How do we trade off the absence of strong form market efficiency—the reason for giving management discretion—and the potential for agency costs, the reason for restraining discretion? The shareholder choice position gives target management the opportunity to reduce the informational inefficiency by seeking alternatives and by disclosing information. Lipton and Rowe's position ignores the agency cost problem and does nothing about the claimed mispricing of a target company's stock.

Neither Lipton and Rowe's position nor my shareholder choice position perfectly solves both problems. Target management may be correct that long-term value is maximized by independence even though it cannot credibly demonstrate it. Alternatively, shareholders may be better off accepting the offer because management's opposition is a mistake or is self-interested. So, how do we choose the best rule for target shareholders?

The question can be posed empirically. Take two samples: one composed of companies that successfully defeated hostile tender offers and remain independent; the second composed of companies that either are taken over by the initial bidder or have secured a better offer. Lipton and Rowe's managerialist position is supported if returns to shareholders of the "remain independent" sample exceed those of the "taken over" sample.

"poison pill." They prefer "Shareholders' Rights Plan." It is hard to see how this label is more descriptive, especially since the thrust of their position in this debate is that shareholders should not have the "right" to forgo a shareholders' rights plan. See Ronald J. Gilson, Just Say No to Whom?, 25 WAKE FOREST L. REV. 121 (1990).
Alternatively, the shareholder choice position is supported if returns to shareholders of the "taken over" sample are higher.

Lipton and Rowe should find this framing of the issue familiar. In Lipton's 1979 article, he undertook a similar empirical test, announcing that a quasi-"remain independent" sample experienced greater returns: "more than 50 percent of the targets are either today at a higher market price than the rejected offer price or were acquired after the tender offer was defeated by another company at a price higher than the offer price."15 The problem was that Lipton's sample included companies that were subsequently acquired at a higher price not long after blocking the hostile offer—an outcome entirely consistent with a shareholder choice regime. If instead the focus is on the subsequent share values of only those companies in Lipton's sample that remained independent, his data reveals a different result. Target shareholders who held on to their shares as a result of management preventing them from tendering in the hostile offer earned an average compounded rate of return on the money they would have received had they been allowed to tender of negative 5.48 percent. This is hardly a testimonial to the value of target management's private information.16

A more recent example of this same phenomenon is set out in Figure One (although it is only one data point, it is a familiar one)—the impact on Time Inc.'s shareholders after the company's ability to stay independent as a result of the Delaware Supreme Court decision that Paul Rowe described as "a promise to corporate America."17 Figure One compares actual post-transaction returns to Time's shareholders with the returns they would have received if they had been allowed to accept Paramount's $200 per share offer and invested the proceeds in either the less risky New York Stock Exchange index or in a debt instrument paying ten percent. It took eleven years for Time's shareholders to break even for the first time, although this condition did not last. Time's shareholders were not wrong in preferring the Paramount offer.

15 Martin Lipton, Takeover Bids in the Target's Boardroom, 35 BUS. LAW. 101, 106 (1979).
16 Gilson, supra note 11.
This analysis suggests that agency cost problems in takeovers are more serious than problems of strong form market inefficiency. This is hardly surprising considering that a shareholder choice approach limits the extent of market inefficiency, while the Lipton and Rowe does nothing to alleviate the agency cost problem.¹⁸

¹⁸Of course, it need not have worked out that way. If one makes strong enough assumptions, any result is possible. For example, Andrei Shleifer and Robert Vishny recently offered a model in which takeover activity in the 1970s, 1980s, and 1990s can be explained by market inefficiency. The model, however, has some Rube Goldberg-like characteristics. First, the stock market is assumed to be dramatically inefficient—either badly over or undervaluing a company's stock—while managers are assumed to be completely rational and understand precisely the way in which the market is inefficient and are also able to predict precisely the long-term value.
There is no need to go into detail in responding to Lipton and Rowe's misstatement of the empirical evidence on takeovers. For present purposes it is sufficient to note that the most recent and extensive empirical investigation, which takes into account the econometric lessons learned from earlier studies, supports the proposition that takeovers result in net shareholder gains, with the lion's share of the gain going to target shareholders. I am not aware of any study that shows other than large positive gains for target shareholders from takeovers.¹⁹

I will pause, however, to question Lipton and Rowe's claim that recent economic challenges to the concept of market efficiency, namely that anomalies such as the January effect, events like the October 1987 market crash, and developments in behavioral economics, render market efficiency an unreliable basis for takeover policy. First, Lipton and Rowe's presentation of this material is strikingly unbalanced.²⁰ More important, however, is their reliance on behavioral economics to undermine the relevance of market efficiency. While Lipton and Rowe point to applications that predict circumstances where the aggregation mechanisms that drive market efficiency may fail, they ignore the fact that the role of shareholders in the governance of takeovers is a trade-off between agency costs and strong form market inefficiency. To evaluate the impact of behavioral economics on this tradeoff requires that we consider its impact on the level of agency costs as well.

Behavioral economics finds its roots in biases identified by cognitive psychologists, especially Amos Tversky and Daniel Kahneman.²¹ These

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¹⁹Gregory Andrade et al., New Evidence and Perspectives on Mergers, 15 J. Econ. Persp. 103 (2001). Lipton and Rowe get a little carried away with their effort to debunk empirical studies supporting shareholder gains from takeovers. They characterize the empirical evidence supporting gains to target shareholders as "weak and inconsistent." Lipton & Rowe, supra note 1, at 21. Here, Lipton and Rowe simply misstate the facts.

²⁰I take some pride in Lipton and Rowe's repeated reference to my discussion of the limits to existing empirical studies of market efficiency. The point is that the evidence on any complex economic phenomenon will be mixed and require analysis. It would have been better had they exhibited similar balance. For an accessible and skeptical discussion of the persuasiveness of recent research on market efficiency, including especially the October 1987 crash and behavioral economics, see Mark Rubinstein, Rational Markets: Yes or No? The Affirmative Case, 57 Fin. ANALYSTS J. 15 (2001).

²¹See, e.g., JUDGMENTS UNDER UNCERTAINTY: HEURISTICS AND BIASES (Daniel Kahneman et al. eds., 1982).
Biases are rooted in failures in individual, not market, decision making, and thus apply more directly to the decision processes of management. For example, suppose we apply cognitive dissonance theory to target management's reaction to a hostile bid which questions management's performance. This suggests that target managers would reduce the dissonance they experience as a result of the hostile bid and its explicit criticism of their performance by deriding the bidders' motives and skills, and acclaiming the bright future under current leadership. While target management might in good faith believe its comments, behavioral economics suggests that the comments grow out of a cognitive bias.

Behavioral economics may in some circumstances predict that the stock market may fail to regress out inaccurate beliefs, but it also predicts dysfunctional defensive behavior by target management in takeovers based on cognitive biases, and in this setting without market aggregation mechanisms to temper them. In the end, behavioral economics speaks to both sides of the trade-off between agency costs and market inefficiency. The necessary judgment remains the same: which failing is systematically worse? My judgment is that behavioral economics will increase the agency cost problem more than it will the strong form market inefficiency problem, reinforcing the shareholder choice position. However, Lipton and Rowe never consider this issue.

II. THE VALUE OF THE POISON PILL

Not surprisingly given Martin Lipton's role as alchemist behind the poison pill, Lipton and Rowe take issue with my proposal that shareholders be allowed to adopt bylaws that amend or repeal board adopted poison pills. They refer to John Coates' careful evaluation of event studies of pill adoptions, and to a number of studies showing that target companies with a poison pill receive higher premiums than target companies without one. Both of these references are said to show that the adoption of a company does not reduce shareholder value.

John Coates' work levels an important criticism of event studies that try to measure the impact on share price of a company's adoption of a poison pill. Coates' point is that because the board of directors can adopt a pill at any time, the company's stock price will already incorporate the pill's expected impact. The actual adoption is therefore not an event.

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Coates' insight, however, says nothing about whether the pill's impact is beneficial to target shareholders; it speaks only to the unreliability of using event studies of the pill's formal adoption to assess its benefit.

The premium studies make a stronger claim—that pills are beneficial to target shareholders because they increase the size of takeover premia. With respect to assessment of this data, the critical fact is that a poison pill is not self-defining. The substance of a pill depends entirely on what the courts allow management to do with it. Suppose a pill only allows management time to secure an alternative transaction and persuade shareholders that the bid price is too low, but does not allow management ultimately to block the offer—call it an Interco pill. The effect of such a pill, then, is to allow management the time to seek a higher bidder. In turn, the premium studies suggest that auctions provide a benefit to target shareholders, an outcome that is precisely what is predicted by the shareholder choice model. If this is what a pill means, as I suggested earlier, it is a useful mechanism to implement a shareholder choice regime, and Lipton, Rowe, and I have no quarrel (although we all may have a quarrel with Easterbrook, Fischel, and Schwartz).

Of course, Lipton and Rowe have a very different view of how target management should be able to use a poison pill. In their view, I assume, management can decline to redeem a pill—to just say no—provided they "show through detailed presentations and expert testimony that their 'assertion' was reasonable and based on appropriate information." Unitrin put the matter somewhat differently. A pill does not need to be redeemed if the refusal is not preclusive; that is, as long as a proxy fight is not "mathematically impossible or realistically unattainable."

The real problem in assessing the impact of the poison pill is framing a clear hypothesis concerning what a pill can accomplish. If companies in fact are adopting Interco pills, one result can be expected. If companies are adopting the Lipton and Rowe "just say no" pills, a different result is expected. Finally, if the substance of pills changes over time because of judicial decisions, and if uncertainty remains over the substance of a pill fifteen years after Household International because the Delaware Supreme Court has declined to clearly state what a pill authorizes management to do, then there is no idea what to expect. The outcome would depend on the

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23Lipton & Rowe, supra note 1, at 31-32. While it would be refreshing for Lipton and Rowe to acknowledge that such a showing was necessary, the reality is that the showing sets a low bar provided that the target company has competent counsel and is actually acting in good faith. Of course, it is possible to trip over even a low bar, as demonstrated by Vice Chancellor Strine's careful opinion in Chesapeake Corp. v. Shore, 771 A.2d 293 (Del. Ch. 2000).

24Unitrin, 651 A.2d at 1388-89.
chronological distribution of the sample and on the degree of uncertainty at any point in time. Any result would necessarily reflect a mix of all these factors, and therefore reveal little about the impact of pill adoption. Without being able to specify the substance of the pills making up the samples of the premium studies, they tell us little about whether a particular version of a poison pill is a good thing or a bad thing for shareholders.25

What does this analysis add to the debate about shareholder choice and shareholder adopted bylaws? I think it reveals what Lipton and Rowe expect shareholders will do if they have the opportunity to act. As I explained in "Unocal Fifteen Years Later," institutional investors will approve sensibly drafted, for example, Interco style, pills and may even approve not so sensibly drafted pills proposed by trusted, well-performing management. I also believe, and the vigor of Lipton and Rowe's response suggests they share this belief, that institutional investors will resist pills that give unimpressive management the power to block a tender offer. Since that position seems perfectly sensible behavior by rational investors, why do Lipton and Rowe object to it? The answer, I think, is a managerialist view of corporate governance that is out of the mainstream; but, of course, they make the very same claim with respect to my views.

In the end, the debate comes back to where it started some twenty years ago—to the allocation of responsibility among shareholders and directors. This brings me to the final point of this response: Lipton and Rowe's claim of a managerialist meta-principle in Delaware corporate law.

III. LIPTON AND ROWE'S MANAGERIALIST META-PRINCIPLE

Lipton and Rowe ultimately transcend their attack on market efficiency and their rigorous defense of the poison pill and thoughtfully confront a serious question: just how managerialist is the DGCL? Whether one views their analysis as a careful apologia for what the Delaware Supreme Court has done but not articulated, or as a road map for what they hope the Delaware Supreme Court will do, this is the right question to ask.

What makes the analysis difficult is the same issue that made it difficult when Lipton wrote on this issue in 1979 and when I responded two years later. The DGCL requires board approval of mergers and sales of assets, thereby giving the board blocking power. The statute was, and remains, silent about tender offers because a tender offer does not require

corporate level action. Lipton in 1979, and now with Rowe, fill that
supposed gap by arguing that a tender offer has the same functional effect
as other fundamental transactions and therefore should be treated the same
way: directors should be able to block a tender offer that they do not
approve. As I suggested in "Unocal Fifteen Years Later," this is a strange
argument for the court that invented the equal dignity doctrine to
rationalize different processes for functionally similar acquisition
techniques. The statute's silence with respect to tender offers, now many
years after their emergence, simply dictates a different process for tender
offers. In 1981, and now, I argue that tender offers provide a critical
safeguard that supports board control over every other acquisition
 technique (and the protection of the business judgment rule). If the board
improperly or mistakenly declines an acquisition offer, the shareholders
can go over their heads by accepting a tender offer. In this analysis, tender
offers are treated differently precisely because they are the functional
equivalent of a merger or sale of assets.

Here, then, is where the issue is joined. In Lipton and Rowe's view,
the role of safety valve that I ascribe to tender offers, they ascribe to
elections: "Shareholder choice’ is exercised in elections for corporate
directors."26 We then confront the comparative advantage of markets and
elections at resolving control contests, which I addressed in "Unocal
Fifteen Years Later."

For present purposes, I will not rehearse the differences in statutory
analysis that both sides to this debate offer to support their positions.
While I think Lipton and Rowe significantly overstate the coherence of the
Delaware statute in this regard and the structural exegesis that has been
offered by the Delaware courts, readers can judge the persuasiveness of the
competing analyses without further assistance from the participants.
Rather, I want to finish by briefly exploring how pervasive Lipton and
Rowe's managerialism is. I suggest that their commitment to elections runs
less deep than they acknowledge, and that their position ends up
threatening the legitimacy of the very system that they (and I) seek to
support.

In "Unocal Fifteen Years Later," I argued that a critical problem with
elections serving as the only safety valve in the system is that defensive
pressure then shifts to elections, and degrades the election process itself.
We have already seen the progression begin—target management is no less
threatened by an election whose campaign theme is to pull the pill than by
the tender offer itself—so that the dynamic we have already observed with

26 Lipton & Rowe, supra note 1, at 26.
defensive tactics is repeated with elections. Counsel devises dead hand and slow hand pills, recommends staggered boards, and formulates tactics, such as eliminating the right of shareholders to call special meetings, and delaying shareholder meetings, which have the unmistaken purpose of shifting the outcome of the election to favor management, irrespective of the merits.

With the welcome exception of Mentor Graphic's dispatch of dead and slow hand pills, the courts have not really policed this process. Lipton and Rowe refer to Chancellor Allen's strict formulation in Blasius—that the "board bears the heavy burden of demonstrating a compelling justification for such [franchise-impairing] action"—as a bulwark against managerial electoral manipulation. It is unclear, however, whether this standard has survived. It seems difficult to rationalize Blasius' requirement that the board demonstrate a compelling justification for manipulating the election process with the Delaware Supreme Court's tepid direction on remand in Unitrin that the chancery court determine only whether the target board's machinations have made a proxy contest "mathematically impossible or realistically unattainable."

Similarly, Vice Chancellor Jacobs' inability to impose limits on board delay of a shareholder called meeting in Mentor Graphics provides further evidence of the difficulty of ensuring the evenhandedness of the electoral process against the weight of determined defensive tactics. Despite the Vice Chancellor's obvious recognition of the potential for abuse, the opinion provides no constraints beyond urging counsel to exercise caution and restraint. As I said in "Unocal Fifteen Years Later," "It is difficult to imagine an electoral process that can both confer legitimacy on the victor and still leave the incumbent very substantial discretion to manipulate the process." There I referred to the first Peruvian presidential election seeking to displace Alberto Fujimoro as providing an example of the corrosive power of scheduling on the legitimacy of elections.

This debate matters because the genius of the American corporate system over the last twenty years has been its ability to quickly adapt to changing economic conditions, assisted in major respects by the ability of those outside the corporation to impose change through the mechanism of

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27Id. at 32 n.130 (quoting Blasts Indus. v. Atlas Corp., 564 A.2d 651, 661 (Del. Ch. 1988)).
29Gilson, supra note 2, at 506.
the market for corporate control. In the early 1990s, a number of critics, including importantly Harvard Business School Professor Michael Porter and Mr. Lipton, compared the U.S. capital market unfavorably to those of Germany and Japan, because of the operation of the market for corporate control. Fifteen years later, the U.S. economy has changed rapidly, reallocating resources by downsizing in some industries and increasing resources devoted to others, accomplished in important respects through the operation of the market for corporate control and through restructurings voluntarily initiated in anticipation of that market. Reflecting this success, international corporate governance reform has followed an explicitly non-managerialist version of the U.S. corporate governance system rather than the much more managerialist systems of Germany and Japan. For example, U.S. style governance reform was an important part of the World Bank's and IMF's response to the 1997-1998 East Asian financial crisis. In the meantime, Japan remains frozen with a corporate governance system that is impervious to external change despite a decade long recession, and the European Union seeks persistently (although with mixed success) to more fully open European corporate governance to external influence.

Lipton and Rowe's response to this concern, I take it, would be that the poison pill and the increasingly managerial bent of Delaware law, exemplified by Unitrin, did not interfere with the remarkable restructuring process the U.S. experienced. But here, however, Lipton and Rowe cannot have it both ways. Lipton and Rowe may be right that the pill did not present a serious barrier because, in the end, the issue of what management could do with the pill was resolved in the market. The views of the institutional investment community made it unlikely that a company ultimately could block shareholders from deciding whether to accept an offer even if the courts might have allowed it. In effect, Lipton and Rowe's point is that the marketplace turned Mr. Lipton's pill into an Interco pill. But if that is right, then all that saved the pill from having a negative economic impact is that it did not function as Lipton and Rowe would have

32 The Report of the High Level Group of Company Law Experts on Issues Related to Takeover Bids (Jan. 20, 2002), which was commissioned by the European Commission following the European Parliament's surprising rejection by a tie vote of the Proposed Thirteenth Directive on takeovers, recommends a new takeover regime that largely embraces the principle of shareholder choice.
liked. And, in that event, it would be helpful if the courts (and Lipton and Rowe) acknowledged that there is no "just say no" defense to tender offers. It has been more than fifteen years since Unocal, and clarity is long overdue.

That leaves us with the problem of repositioning Delaware law with the assumption that the Delaware Supreme Court will prove characteristically reluctant to reconsider its doctrinal construct.33 Allowing shareholders, by initiating bylaws, a hand in assuring that the design of a poison pill actually benefits them, is a workable, if only partial solution that finds its support in the language of the DGCL and in the Delaware Supreme Court's penchant for according each statutory provision equal dignity. It would also take the pressure off of the electoral process and eliminate the embarrassing spectacle of directors manipulating their own election.

33 In a remarkable recent article, the former Chancellor and two sitting Vice Chancellors set out an extra judicial road map for how the Delaware Supreme Court might usefully uncomplicate its takeover doctrine. William T. Allen et al., Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law, 56 Bus. LAW. 1287 (2001). While their proposals are quite moderate, the Delaware Supreme Court has evidenced no inclination to follow their advice. See A. Gilbert Sparks & Patricia R. Uhlenbrock, Progress Update: Delaware's Common Law Simplification Initiative (Jan. 2002) (manuscript on file with author).