TAKEOVER DEFENSE STRATEGIES

1. Poison pill is a strategy that tries to create a shield against a takeover bid by another company by triggering a new, prohibitive cost that must be paid after the takeover.
There are many poison pill strategies that have been used by companies against hostile takeovers and corporate raiders. For example, offering a preferred stock option to current shareholders allows them to exercise their purchase rights at a huge premium to the company, making the cost of the acquisition suddenly unattractive. Another method is to take on a debt that would leave the company overleveraged and potentially unprofitable.
Some companies have created employee stock ownership plans that vest only when the takeover is finalized. In addition to a dilution of the stock value, such employee benefits may result in an employee exodus from the company leaving it without its talented workforce (which is often one of the drivers of the acquisition).
Another example is to offer a series of golden parachutes for company executives. This could also make the takeover of the company prohibitively expensive the buyer had planned to replace the top management.
Finally, one non-financial method of a poison pill is to stagger the election of the board of a company, causing the acquiring company to face a hostile board for a prolonged period of time. In some cases, this delay in gaining control of the board (and therefore the votes necessary to approve certain key actions) is a sufficient deterrent for a takeover attempt. An extreme implementation of a poison pill is called a suicide pill.

Poison pills raise the cost of mergers and acquisitions. At times, they create enough of a disincentive to deter takeover attempts altogether. Companies should be careful, however, in constructing poison pill strategies. As a strategy, poison pills are only effective as a deterrent. When actually put into effect, they often create potentially devastatingly high costs and are usually not in the best long-term interests of the shareholders.
Defensive tactics that make hostile takeover by a corporate-raider prohibitively expensive or unattractive. Poison pill takes several forms: (1) provision that makes the firm's all debts immediately payable if the board of directors is changed; (2) distribution of warrants or purchase rights for buying the firm's stock (shares) at a heavy (usually 50 percent) discount when a triggering event (takeover attempt) occurs, thus immediately diluting the raider's ownership interest and voting rights; and/or (3) issuance of a new series of preferred stock (preference shares) that gives stockholders/shareholders (not including the raider) right to redeem them at a hefty premium after a takeover.

2. Greenmail is an acquisition tactic whereby the acquirer attempts to obtain a controlling interest in a target by buying shares at a premium from the target's shareholders.
Let's assume an entity that Company XYZ considers unsavory (we'll call it Party X) is attempting to acquire control of Company XYZ by offering to buy shares at a premium from Company XYZ's shareholders. To avoid being purchased by Party X, Company XYZ's board of directors might offer to purchase Party X's shares for a price above the current market price. This of course makes Party X go away (and a lot richer, by the way), but the transaction can also be construed as Party X blackmailing (or greenmailing) Company XYZ by threatening to take over the company if it does not pay a particular premium to Party X. To avoid this situation, in which Company XYZ might make an offer to repurchase shares at a price above what other shareholders might get, anti-greenmail provisions exist. These provisions generally state that if Company XYZ pays a premium to repurchase shares, it must offer that premium to all shareholders. An anti-greenmail provision is a clause in a corporation's charter that deters thecorporation's board from conducting a stock buyback. Company XYZ does this in exchange for Party X's agreement not to attempt to acquire the company for a period of time. Anti-greenmail provisions are attempts to thwart takeover threats from speculators, disruptive shareholders, and "unsavory" entities that are seeking a payoff rather than a genuine business relationship. In general, a corporation's shareholders must vote to adopt or abandon anti-greenmail provisions.

3. A **golden parachute** is an agreement between a company and an employee (usually a high level executive) that provides significant financial benefits to the employee upon termination.
For example, upon a change in ownership or a shake-up in management, a *golden parachute* clause in an executive's employment contract might specify that the executive will be granted special severance pay, bonuses, stock options, or other non-cash benefits upon his departure from the organization. Theoretically, since the executive's own financial future is protected, he or she is free to make decisions about reorganizations, mergers or sell-offs that are in the long-term best interests of the company, even though such actions may lead to his or her dismissal.
Golden parachutes are meant to help companies hire and retain top talent. At the same time, golden parachutes have increased compensation costs, which can pose an obstacle to a transaction.

4. Companies adopt a **macaroni defense** by issuing bonds that are redeemable at a high price in the event of a change in control.
For example, let's assume that Company ABC wants to buy Company XYZ. Company XYZ doesn't want to sell because in the board's opinion Company ABC makes terrible products and will run the company's brand into the ground. To thwart the effort, Company XYZ issues $10 million of bonds that are redeemable for 150% of par value if there is a change in control at Company XYZ. So, a person who buys a Company XYZbond with a $1,000 face value would have the right to redeem that bond for $1,500 if Company ABC buys Company XYZ. Company ABC, seeing this redemption as a cost on top of buying Company XYZ, backs off the deal.
Like pasta in water, the bonds involved in a macaroni defense expand when things get hot. For potential acquirers, this can make a deal very hard to swallow.

5. A **white knight** is a company that acquires another company that is trying to avoid acquisition by a third party.
For example, let's assume that Company XYZ wants to acquire Company ABC. Company ABC feels that Company XYZ is a hostile bidder and will ruin the company. As a result, Company ABC's directors go on the offensive and tell the shareholders that a sale to Company XYZ would not be a good thing. Company 123, which has worked with Company ABC for years and has a good relationship with its board, sees an opportunity to "save" Company ABC from the tense situation and make a lucrative acquisition at the same time. Company ABC welcomes Company 123's bid and merges with it to avoid acquisition by Company XYZ. Company 123 is a white knight.
White knights make acquisitions on friendly terms. White knights are white because they are associated with goodness and virtue. The white knight is the "savior" of a company in the midst of a hostile takeover. Often a white knight is sought out by company officials - sometimes to preserve the company's core business and other times just to negotiate better takeover terms. An example of the former can be seen in the movie "Pretty Woman" when corporate raider/black knight Edward Lewis (played by Richard Gere) has a change of heart and decides to work with the head of a company he'd originally planned on ransacking. In addition to white knights and black knights, there is a third potential takeover candidate called a gray knight. As one might guess, a gray knight is not as desirable as a white knight, but more desirable than a black knight.

6. A **Pac-Man defense** is a strategy for averting hostile takeovers.
Let's assume Company ABC wants to purchase Company XYZ. Company XYZ's board does not want to sell, but Company ABC threatens a hostile takeover. To ward off the takeover attempt, Company XYZ makes an offer to buy Company ABC. In the popular 1980s video game, Pac-Man is able to eat a power pellet that gives him the power to eat the ghosts that are chasing him. Martin Marietta Corporation introduced the Pac-Man defense in 1982 by bidding for every company that was trying to buy it.
The Pac-Man defense is a drastic step because it often requires targets to borrow or dip into cash to purchase potential acquirers.

7. A **sale of crown jewels** occurs when a company is frantically attempting to fend off a takeover.
For example, Company ABC makes a bid to buy Company XYZ. Company XYZ's founder, who is the chairman of the board, absolutely abhors Company ABC and refuses to sell the company to them. Company ABC goes directly to the Company XYZ shareholders and offers to buy their shares for a 10% premium. Fearful that Company ABC may be successful in its efforts, Company XYZ intentionally hurts the value of the company by selling its key intellectual property (the "crown jewels") to the founder. Without these assets, the company is worth far less. Company XYZ also ceases advertising, breaks supplier agreements in order to slow down production and lays off 2,000 workers. With key aspects of the company gutted and the most valuable assets gone, Company ABC drops its bid for Company XYZ, which is now a hollow, valueless shell of its former self.
Selling the crown jewels is near suicide -- the board has to be willing to nearly kill the company in order to save it from acquisition. This is very risky, and in some cases the shareholders will oppose the effort. For this reason, selling the crown jewels is often a last resort.

8. **People Pill:** A defensive strategy to ward off a hostile takeover. The target company's management team threatens that, in the event of a takeover, the entire team will resign. The purpose of a people pill is to discourage the acquiring company from completing the takeover, by introducing the possibility of having to put together an entirely new management team. This strategy is only effective if the acquiring company wants to keep the existing management.
The first use of the people pill anti-takeover strategy is attributed to a food company called the Borden Corporation. In 1989, the company's board of directors approved a people pill that Borden could use to demand that an acquiring company pay a fair value for the company's shares and that it not fire or demote any of Borden's existing managers.

The people pill strategy is a variation of the poison pill defense. Other takeover defenses include staggered boards, golden parachutes and shareholder rights plans.

9. **Yellow Knight:** A company that was once making a takeover attempt but ends up discussing a merger with the target company. Yellow knights have various reasons for backing out of the takeover attempt, but frequently are attributable to the target company's ability to fend off takeover. The "yellow" in "yellow knight" may refer to the color's association with cowardice. Since a yellow knight backs down from a takeover attempt and retreats to merger discussions, a yellow knight may be viewed as weak.
In mergers and acquisitions (M&A), various colored knights are used to identify the nature of a takeover or potential takeover. A black knight is a company that makes a hostile takeover offer for the target company. A white knight makes a friendly takeover offer to a target company that is being faced with a hostile takeover. A gray knight (sometimes spelled grey knight) is a second unsolicited bidder in a corporate takeover.

10. **'White Squire'**: Very similar to a "white knight", but instead of purchasing a majority interest, the squire purchases a lesser interest in the target firm.
A white squire is still considered to be a friendly acquirer, they just don't require controlling interest like a "white knight" does.

11**. Sandbag** is a tactic used to hide or limit expectations of a company's or individual's strength in order to produce greater than anticipated results. Sand bagging, in business, is most often seen when company managers temper the expectations of superiors or shareholders by giving guidance below what they know will be achieved. Once the better than expected results are presented, the firm looks all the better.
Let's imagine for example that Orange Inc had gained a reputation in the late 2000s for sandbagging quarterly expectations leading up to earnings season. Analysts and pundits alike would be confident that quarterly numbers would be strong. However, when results were released they would be markedly higher than most expected, thus leading to a surge in share value, which may be a more favorable outcome in terms of press coverage.

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Bear hug: is an offer made by one company to buy the shares of another for a much higher per-share price than what that company is worth. A bear hug offer is usually made when there is doubt that the target company's management will be willing to sell. The name "bear hug" reflects the persuasiveness of the offering company's overly generous offer to the target company. By offering a price far in excess of the target company's current value, the offering party can usually obtain an agreement. The target company's management is essentially forced to accept such a generous offer because it is legally obligated to look out for the best interests of its shareholders.

Leveraged Buyout - LBO': A leveraged buyout (LBO) is the acquisition of another company using a significant amount of borrowed money (bonds or loans) to meet thecost of acquisition. Often, the assets of the company being acquired are used as collateral for the loans in addition to the assets of the acquiring company. The purpose of leveraged buyouts is to allow companies to make large acquisitions without having to commit a lot of capital. In an LBO, there is usually a ratio of 90% debt to 10% equity. Because of this high debt/equity ratio, the bonds usually are not investment grade and are referred to asjunk bonds. Leveraged buyouts have had a notorious history, especially in the 1980s when several prominent buyouts led to the eventual bankruptcy of the acquired companies. This was mainly due to the fact that the leverage ratio was nearly 100% and the interest payments were so large that the company's operating cash flows were unable to meet the obligation. It can be considered ironic that a company's success (in the form of assets on the balance sheet) can be used against it as collateral by a hostile company that acquires it. For this reason, some regard LBOs as an especially ruthless, predatory tactic.

Bailout Takeover': A scenario in which a government or profitable company acquires control of a financially unstable company with the goal of returning it to a position of financial strength. In a bailout takeover, the government or strong company takes over the weak company by purchasing its shares, exchanging shares or both. The acquiring entity develops a rehabilitation plan for the weak company, describing how it will be managed and by whom, how shareholders will be protected and how its financial position will be turned around. An example of a bailout takeover is the U.S. government's takeover of Chrysler and General Motors in 2008 to prevent the companies' bankruptcy and the subsequent loss of approximately 1 million jobs in the industry. Under the takeover's terms, the government

loaned the two companies $17.4 billion and required them to reduce debt, decrease workers' wages and benefits, and create restructuring plans.

Dawn Raid': A dawn raid is when a firm or investor buys a substantial number of shares in a company first thing in the morning when the stock markets open. Because the bidding company builds a substantial stake in its target at the prevailing stock market price, the takeover costs are likely to be significantly lower than they would be had the acquiring company first made a formal takeover bid. Like the dawn raid in war, the corporate dawn raid is done early in the morning, so by the time the target realizes it's being attacked, it's too late - the investor has already scooped up some controlling interest. However, only a minority interest in a firm's shares can be bought this way. So, after a successful dawn raid, the raiding firm is likely to make a takeover bid to acquire the rest of the target company.

Saturday Night Special': An obsolete takeover strategy where one company attempted a takeover of another company by making a sudden public tender offer, usually over the weekend. This merger and acquisition (M&A) technique was popular in the early 1970s when the Williams Act required only seven calendar days between the time that a tender was publicly announced and its deadline. Catching the target company off guard and over the weekend, effectively reducing its time for a response, often afforded the acquiring company an advantage. A tender offer is basically an attempt to takeover control of a company by asking shareholders to sell their shares at a specified price (usually above market). If enough shareholders sell their shares, the takeover is complete. The Saturday Night Special was effective when the Williams Act required a minimum of seven days between the public announcement of the tender and its deadline. When the time period was extended to 20 days, this technique failed to be the quick strike it was originally intended to be. In addition, acquisitions of 5% or more of equity now need to be disclosed to the Securities Exchange Commission (SEC).

Friendly Takeover': A situation in which a target company's management and board of directors agree to a mergeror acquisition by another company. In a friendly takeover, a public offer of stock or cash is made by the acquiring firm, and the board of the target firm will publicly approve the buyoutterms, which may yet be subject to shareholder or regulatory approval. This stands in contrast to a hostile takeover, where the company being acquired does not approve of the buyout and fights against the acquisition. In most cases, if the board approves a buyout offer from an acquiring firm, the shareholders will vote to pass it as well. The key determinant in whether the buyout will occur is the price per share being offered. The acquiring company will offer a premium to the current market price, but the size of this premium (given the company's growth prospects) will determine the overall support for the buyout within the target company.

Hostile Takeover': A hostile takeover is the acquisition of one company (called the target company) by another (called the acquirer) that is accomplished not by coming to an agreement with the target company's management, but by going directly to the company's shareholders or fighting to replace management in order to get the acquisition approved. A hostile takeover can be accomplished through either a tender offer or a proxy fight. The key characteristic of a hostile takeover is that the target company's management does not want the deal to go through. Sometimes a company's management will defend against unwanted hostile takeovers by using several controversial strategies including the poison pill, crown-jewel defence, golden parachute, pac-man defence, and others.