TAKEOVER DEFENSES

Poison Pill Plans Are Popping
(M&A Tax Report)

Not always the shareholders' right. To date, over 2,000 public companies have implemented poison pill plans to deter unwanted suitors from taking over their stock and control. Under most poison pills, receiving an unwanted bid triggers an enormous issuance of stock, which makes a buyout much more expensive for the bidder. Not many of these plans are put to a vote of the shareholders, since some antitakeover actions serve to stabilize weak management even though shareholders may favor the suitor's bid. Last year, corporate shareholders brought initiatives for more control over the company's use or the existence of poison pills at 18 companies and won 55% of the votes.

A different pill. At Texaco's recent annual meeting, management presented a so-called shareholders' rights plan. Not only was bringing the plan to a vote unusual, but also many features of the plan were unique. First, the trigger for implementing the plan is an offer for 20% of the company's stock, rather than the 5% or 10% more commonly seen. Second, the plan has only a five-year life rather than the more usual term of 10 years. Third, the plan is "chewable" (i.e., it dissolves) if all shareholders receive a cash tender offer for their shares. Texaco management encouraged shareholders to adopt the plan by saying the plan insures that no suitor can acquire a controlling interest in Texaco, a company with an enormous market capitalization, unless the deal benefits all the shareholders.

Poison pills appear tax-neutral. In a 1990 revenue ruling, the IRS concluded that a poison pill generally does not create income, since the trigger is contingent upon a tender offer or acquisition, and does not constitute an option. Although the ruling was based on a specific plan, the basic analysis should hold for similar plans. These plans have, at their core, a right offered to shareholders to buy stock at a discount, in response to a suitor's offer. Seemingly easy provisions to duplicate, but unknown tax elements remain. Whether the company must include a termination right is not clarified in the ruling. The plan in question allowed management to cancel the plan for several days after the rights were distributed, for minor compensation paid to the shareholders. Shareholders would certainly be unhappy if they were taxed on those rights. After all, they may have had no say in whether to battle against an offer that may, in fact, be above market value.

More Poison Pill Plans, by Robert Wood. ***M&A Tax Report,*** June 1998, Pgs. 1, 3-4. Tax Institute, 235 Montgomery St., No. 972, San Francisco, CA 94104. Poison pills are also featured in July *M&A Tax Report*. ■