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Reliance Requirement for a Non-Tendering Shareholder

TENDER OFFERS: STANDING TO SUE, PROHIBITED PRACTICES, RELIANCE OF NON-TENDERER

Congress passed the Williams Act[1] in 1968 to control and regulate the growing use of tender offers[2] as a means of gaining corporate control.[3]

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[1] Williams Act, *adding* Securities Exchange Act of 1934 §§ 13(d)-(e), 14(d)-(f), 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1976 & Supp. II 1978) [hereinafter cited as Williams Act].

[2] Congress did not define "tender offer" in the Williams Act. *See* M. LIPTON & E. STEINBERGER, TAKEOVERS AND FREEZEOUTS § 2.3.1 (1978) [hereinafter cited as LIPTON & STEINBERGER]. Until recently, the Securities and Exchange Commission (SEC) also declined to define "tender offer." *See* SEC Securities Exchange Act Release No. 34-12676 (Aug. 2, 1976) [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,659 at 86,695-96; E. ARANOW, H. EINHORN & G. BERLSTEIN, DEVELOPMENTS IN TENDER OFFERS FOR CORPORATE CONTROL 1-3 (1977) [hereinafter cited as ARANOW, EINHORN & BERLSTEIN]. On November 29, 1979, however, the SEC published Proposed Rule 14d-1 to amend 17 C.F.R. § 240 (1979) by providing a concrete definition of a tender offer. *See* Note, *What is a Tender Offer?* 37 WASH. & LEE L. REV. 908 (1980).

The flexibility of the tender offer as a means to gain corporate control helps explain the tender offer's popularity. A tender offer is available to acquire a company that opposes acquisition, to effect an acquisiton that is not opposed but which a majority of the board of directors does not want to sponsor, to acquire control of a target before a third party can perfect a competing offer, and to rescue a company in trouble when insufficient time exists for a merger. *See* LIPTON & STEINBERGER, *supra* § 1.1.1.

[3] Prior to the adoption of the Williams Act, little regulation governed the mechanics and techniques used in executing a tender offer. *See* Pitt, *Standing To Sue Under the Williams Act After* Chris-Craft; *A Leaking Ship on Troubled Waters,* 34 BUS. LAW. 117, 125 (1978) [hereinafter cited as Pitt]. The relatively few state laws governing tender offers were ineffective, and virtually no federal securities law covered this method of gaining corporate control. *Id.* Congress passed the Williams Act to alleviate the inadequacy in the federal regulatory scheme. *See* Piper v. Chris-Craft Indus., Inc., 430 U.S. 1, 22 (1977).

The need to correct the inadequacy in the federal securities laws was highlighted during the 1960's by the dramatic increase in the use of tender offers as a means of facilitating a corporate takeover. *See id.* at 22; E. ARANOW & H. EINHORN, TENDER OFFERS FOR CORPORATE CONTROL 64-65 (1973) [hereinafter cited as ARANOW & EINHORN]; Note, *1977-1978 Securities Law Developments: Tender Offers,* 35 WASH. & LEE L. REV. 893, 893 (1978) [hereinafter cited as *Tender Offers*]. Tender offers involving companies listed on national securities exchanges jumped from 8 in 1960 to 107 in 1966. ARANOW & EINHORN, *supra* at 65 n.3. The eight tender offers in 1960 were for $200 million of listed securities. *Id.* This figure rose to approximately $1 billion in 1965. *Id. see* 113 CONG. REC. 24662-64 (1967).

Federal regulation of tender offers originally was proposed in 1965 by Senator Harrison Williams of New Jersey. ARANOW & EINHORN, *supra* at 64. The original bill sought to protect established companies from "industrial sabotage" resulting from tender offers. *Id.; see* 111 CONG. REC. 28256-60 (1965). Hearings were not held on the original bill but many of the bill's precepts formed the basis for a second bill introduced by Senator Williams in 1967. ARANOW & EINHORN, *supra* at 66. By 1966, however, Congress recognized that tender offers are beneficial in appropriate circumstances because they provide a method of removing entrenched but ineffective management. *Id.; see* Pitt *supra* at 127. Hence, the final form of the Williams Act, effective on July 29, 1968, was neutral in that the Act favored neither the tender offeror nor the management of the target company. ARANOW & EINHORN, *supra* at 67; *see* H.R. REP. NO. 1711, 90th Cong., 2d Sess., *reprinted in* [1968] U.S. CODE CONG. & AD.

The Williams Act seeks to provide full and fair disclosure of all pertinent information[4] to the investor faced with a tender offer.[5] The Act insures full and fair disclosure by requiring the filing of a statement by a tender offeror with the Securities and Exchange Commission (SEC) when the tender offer is made.[6] Within ten days after acquiring beneficial ownership[7] of five percent of any class of a target company's registered equity securities, a tender offeror must file an additional statement with the SEC, the target corporation, and any exchange on which the target's securities are traded.[8] Further, the Williams Act broadly proscribes material misstatements, misleading omissions, and fraudulent or manipulative acts in connection with tender offers.[9]

Although Congress did not provide explicitly for private enforcement of the Williams Act, courts have not hesitated to imply private causes of action.[10] In implying private causes of action, however, the courts have had difficulty defining the standing requirements for private plaintiffs.[11] Furthermore, the broad anti-fraud provision[12] has created confusion as to

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NEWS 2811, 2813. Thus, the Williams Act requires full and fair disclosure for the benefit of investors while, at the same time, providing the offeror and the target's management an equal opportunity to present their cases.

[4] *See* text accompanying notes 7-8 *infra.*

[5] *See* H.R. REP. No. 1711, 90th Cong., 2d Sess., *reprinted in* [1968] U.S. CODE CONG. & AD. NEWS 2811, 2813; note 3 *supra.*

[6] 15 U.S.C. § 78m(d) (Supp. II 1978). The tender offeror must file a disclosure statement, Schedule 14D-1, when the offeror would own more than five percent of a class of a target corporation's registered securities as a result of the tender offer. *See id.*; 17 C.F.R. § 240.14d-100 (1979). Schedule 14D-1 must contain information regarding the identity and background of the tender offeror, the source of funds for the tender offer, and any plans or proposals for mergers, acquisitions, or other major changes in the target company's corporate structure. *See* 15 U.S.C. § 78n(d) (1976). Section 78n also delineates withdrawal rights with respect to tendered shares, *id.* § 78n(d)(5), requirements as to pro rata acceptance when more shares are tendered than sought, *id.* § 78n(d)(6), and obligations of the offeror when changes are made in the terms of the offer. *Id.* § 78n(d)(7).

[7] The beneficial owner of a security is any person who directly or indirectly has the voting power and/or the investment power of that security. SEC Securities Exchange Act Release No. 34-13291 (Feb. 24, 1977) [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,980 at 87,577. Voting power includes the power to vote or direct the voting of the security. *Id.* Investment power includes the power to dispose or direct the disposition of the security. *Id.*

[8] 15 U.S.C. § 78m(d)(1) (Supp. II 1978). The statement which the tender offeror must file after acquiring the beneficial ownership of five percent of any class of the target company's registered equity securities is a Schedule 13D. *See* 17 C.F.R. § 240.13d-1 (1979). Schedules 13D and 14D-1, *see* note 6 *supra*, contain basically the same information. *See* 15 U.S.C. §§ 78m(d)(1), 78n(d) (1976 & Supp. II 1978). *See also Tender Offers, supra* note 3, at 894.

[9] 15 U.S.C. § 78n(e) (1976); *see* note 15 *infra.*

[10] *See, e.g.*, Sargent v. Genesco, Inc., 492 F.2d 750, 769 (5th Cir. 1974); Smallwood v. Pearl Brewing Co., 489 F.2d 579, 596 n.20 (5th Cir.), *cert. denied*, 419 U.S. 873 (1974); Reserve Management Corp. v. Anchor Daily Income Fund, Inc., 459 F. Supp. 597, 607 (S.D.N.Y. 1978).

[11] *See* text accompanying notes 15-69 *infra.*

[12] *See* text accompanying note 9 *supra*; note 15 *infra.*

when and to what practices the Williams Act applies.[13] Finally, the courts have had to decide whether a non-tendering shareholder must establish reliance to recover damages under the Williams Act.[14]

A. *Standing to Sue Under the Williams Act*

Section 14(e)[15] of the Securities Exchange Act of 1934 ('34 Act) is the broad anti-fraud provision that provides the basis for most of the private litigation instituted under the Williams Act.[16] Since section 14(e) does not provide expressly for a private cause of action,[17] the courts have had to define the standing requirements for a plaintiff in a private suit brought for alleged tender offer violations.[18] In *Hundahl v. United Benefit Life Insurance Co.*,[19] the court held that a non-tendering shareholder of the target corporation has standing to bring suit based on a violation of section 14(e).[20]

Hundahl involved a tender offer by Mutual of Omaha Insurance Company (Mutual) for 8.51 percent of the stock of United Benefit Life Insurance Company (United).[21] Plaintiffs, shareholders of United,[22] sued under section 14(e)[23] two days before the expiration of Mutual's tender offer

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[13] *See* text accompanying notes 70-174 *infra*.

[14] *See* text accompanying notes 175-97 *infra*.

[15] 15 U.S.C. § 78n(e) (1976). Section 14(e) provides in pertinent part:

> It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made. . .not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders. . . .

[16] Rule 10b-5 is the broad anti-fraud provision that prevents misleading statements, material omissions, and fraudulent or manipulative practices in connection with the purchase or sale of any security. *See* 17 C.F.R. § 240.10b-5 (1979). Section 14(e) contains the same basic language as Rule 10b-5 and thus, in effect, applies Rule 10b-5 to tender offers. *See* Golub v. PPD Corp., 576 F.2d 759, 764 (8th Cir. 1978); Smallwood v. Pearl Brewing Co., 489 F.2d 579, 605-06 (5th Cir. 1974); Electronic Specialty Co. v. International Controls Corp., 409 F.2d 937, 940 (2d Cir. 1969); Applied Digital Data Systems Inc. v. Milgo Elec. Corp., 425 F. Supp. 1145, 1157 (S.D.N.Y. 1977); Hurwitz v. R.B. Jones Corp., 76 F.R.D. 149, 161 (W.D. Mo. 1977).

[17] *See* note 15 *supra*.

[18] *See* text accompanying notes 15-69 *infra*.

[19] 465 F. Supp. 1349 (N.D. Tex. 1979).

[20] *Id.* at 1368. *See also In re* Commonwealth Oil/Tesoro Petroleum Corp. Sec. Litigation, 467 F. Supp. 227, 242 (W.D. Tex. 1979) (non-tendering shareholder of target corporation has standing to sue for alleged violation of § 14(e)); text accompanying notes 155-74 *infra*.

[21] 465 F. Supp. at 1353.

[22] The plaintiffs in *Hundahl*, with respect to the § 14(e) claim, sued individually as shareholders of United Benefit Life Insurance Company (United) and as representatives of a class composed of all current minority shareholders of United. *See id.*

[23] The plaintiffs in *Hundahl* also alleged a violation of Rule 10b-5. *See id.* at 1356-66. Because of the similarity between § 14(e) and Rule 10b-5, *see* note 16 *supra*, suits brought for fraudulent and deceptive conduct in connection with a tender offer may contain claims based on violations of both provisions.

and sought injunctive and monetary relief.[24] Plaintiffs had not tendered any of their United shares in response to Mutual's offer.[25] The *Hundahl* court thus faced the question of whether an implied cause of action exists under section 14(e) in favor of a non-tendering shareholder of the target corporation.[26]

In *Piper v. Chris-Craft Industries, Inc.*,[27] the seminal case involving standing to sue under section 14(e), the Supreme Court held that a defeated tender offeror lacked standing under section 14(e).[28] An examination of the legislative history of section 14(e) led the Court to conclude that Congress enacted the Williams Act solely for the protection of investors confronted with a tender offer and not for defeated tender offerors such as Chris-Craft.[29] The Court reasoned that implying a private cause of action in favor of a defeated tender offeror would not further the congressional goal of protecting the investor.[30] Moreover, since Chris-Craft's claim was cognizable under state law, no need existed for creating a federal cause of action.[31]

The *Hundahl* court adopted the *Chris-Craft* analysis to determine whether section 14(e) creates a private cause of action for a target company's shareholder.[32] After examining the legislative history of section

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[24] 465 F. Supp. at 1353.

[25] *Id.* at 1366.

[26] *Id.*

[27] 430 U.S. 1 (1977). Chris-Craft Industries, Inc. (Chris-Craft) sought to gain voting control of Piper Aircraft Corp. (Piper) through a series of cash and exchange tender offers. *Id.* at 5-7. Piper's management opposed the tender offer and arranged to work with Bangor Punta Corporation (Bangor Punta) to prevent the takeover by Chris-Craft. *Id.* at 6-7. The combined efforts of Piper and Bangor Punta prevented Chris-Craft's takeover bid. *Id.* at 9. Chris-Craft sued alleging material misstatements and omissions during the tender offer amounting to a violation of § 14(e). *Id.* at 17.

[28] *Id.* at 42. The Supreme Court denied Chris-Craft standing to bring suit as a defeated tender offeror despite the fact that Chris-Craft was also a shareholder of Piper, the target corporation.

[29] *Id.* at 26-35. Whether a federal statute creates a private cause of action for a particular plaintiff depends on whether Congress intended to create the private right asserted. *See* Transamerica Mortgage Advisors, Inc. v. Lewis, 444 U.S. 11, 14 (1979); Touche Ross & Co. v. Redington, 442 U.S. 560, 568 (1979).

[30] 430 U.S. at 39-40. The court in *Chris-Craft* stated that a damage award to a defeated tender offeror would not benefit the target corporation's shareholders, the intended beneficiaries of the Williams Act, but would benefit one of the parties regulated by the legislation. *Id.* at 39. Further, the threat of damages against a successful contestant in a battle for corporate control would not protect investors to a significant degree. *Id.* at 39-40. In fact, tender offerors might not make some tender offers, to the detriment of investors, if the successful tender offeror faces a suit for massive damages brought by a defeated tender offeror. *Id.* at 40; *cf.* Cort v. Ash, 422 U.S. 66, 80-85 (1975) (statement of tests used by *Chris-Craft* Court to determine whether to imply private cause of action).

[31] 430 U.S. at 40-41. Chris-Craft's complaint stated a cause of action under common law principles for interference with a prospective commercial advantage, a cause of action traditionally brought under state law. *Id.*

[32] *See* 465 F. Supp. at 1366-70. The *Chris-Craft* Court specifically left open the question of whether § 14(e) creates a private cause of action for a target company's shareholder.

14(e), the *Hundahl* court concluded that Congress enacted section 14(e) solely for the protection of shareholders of the target corporation.[33] Therefore, any monetary award resulting from such an action would benefit those protected by the statute.[34] In addition, section 14(e) contains the same basic language as Rule 10b-5,[35] and Congress, in enacting section 14(e), knew that courts often had implied private causes of action under Rule 10b-5.[36] Finally, the *Hundahl* court stated that the creation of a private damages remedy was necessary to effectuate the purposes of the Williams Act because the SEC is not involved in the early stages of takeover activity and injunctive relief is often impracticable.[37]

Hundahl further extended the implied cause of action under section 14(e) to non-tendering shareholders of a target corporation.[38] The court emphasized that section 14(e), unlike Rule 10b-5,[39] applies whether or not the plaintiff has purchased or sold securities.[40] The omission of a purchaser-seller requirement in section 14(e), according to the *Hundahl* court, indicates a congressional intent not to require a tendering of shares before a shareholder of the target corporation can take advantage of sec-

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See 430 U.S. at 42 n.28.

[33] 465 F. Supp. at 1367; *see* 113 CONG. REC. 854 (1967) (legislation will close significant gap in investor protection under federal securities laws by requiring disclosure of pertinent information to stockholders); 113 CONG. REC. 24664 (1967) (Williams Act is designed solely to require full and fair disclosure for benefit of investors). The *Hundahl* court also noted that Congress enacted the Williams Act to avoid aiding either the target corporation's management or the tender offeror in a takeover bid. 465 F. Supp. at 1367. *Chris-Craft* held that this purpose of the Williams Act prevented implying a cause of action in favor of a tender offeror because implication of a private right would disrupt the "evenhandedness" created by the Act. 430 U.S. at 31. *Hundahl* held that implying a cause of action in favor of a target shareholder would not upset the Williams Act's evenhandedness because the shareholder of the target corporation is the express beneficiary of the statute. 465 F. Supp. at 1367.

[34] 465 F. Supp. at 1367. The *Chris-Craft* Court, in holding that § 14(e) does not create a private cause of action in favor of a defeated tender offeror, stated that any award of damages to a defeated tender offeror would not benefit the investors who are the intended beneficiaries of § 14(e). *See* 430 U.S. at 39; note 30 *supra*. The *Hundahl* court interpreted this statement in *Chris-Craft* to imply that an award of damages benefiting the intended beneficiary of § 14(e) is acceptable. *See* 465 F. Supp. at 1367.

[35] *See* note 16 *supra*.

[36] 465 F. Supp. at 1367.

[37] *Id.; see* Pitt, *supra* note 3, at 163-66. The lower courts uniformly hold that an implied cause of action in favor of shareholders of the target company exists under § 14(e). *See, e.g.*, Indiana Nat'l Bank v. Mobil Oil Corp., 578 F.2d 180, 183 n.5 (7th Cir. 1978); Sargent v. Genesco, Inc., 492 F.2d 750, 769 (5th Cir. 1974); Smallwood v. Pearl Brewing Co., 489 F.2d 579, 596 (6th Cir. 1974); Reserve Management Corp. v. Anchor Daily Income Fund, Inc., 459 F. Supp. 597, 607 (S.D.N.Y. 1978).

[38] 465 F. Supp. at 1367.

[39] *See* note 16 *supra*.

[40] 435 F. Supp. at 1368 (quoting Smallwood v. Pearl Brewing Co., 489 F.2d 579, 596 (5th Cir. 1974)). Rule 10b-5 prohibits manipulation and deception in the purchase and sale of securities. *See* 17 C.F.R. § 240.10b-5 (1979); note 16 *supra*. Courts construe this purchaser-seller requirement to mean that a plaintiff must be a purchaser and seller of securities in order to have standing to sue under Rule 10b-5. *See, e.g.*, Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 731, 749 (1975); note 41 *infra*.

tion 14(e)'s protections.[41]

The *Hundahl* decision to imply a section 14(e) cause of action in favor of a non-tendering shareholder is correct. All of the target company's shareholders must decide whether to accept a tender offer. The legislative history of the entire Williams Act indicates that Congress intended the benefits of the Act to accrue to shareholders of the target corporation.[42] No distinction is made between tendering and non-tendering shareholders. In fact, the absence of a purchaser-seller requirement in section 14(e) clearly indicates that Congress specifically contemplated the protection of the non-tendering shareholder.[43] Moreover, the Supreme Court has intimated support for the *Hundahl* decision to extend standing under section 14(e) to a non-tendering target shareholder.[44]

Like the court in *Hundahl*, the Second Circuit, in *Crane Co. v. American Standard, Inc.*,[45] decided whether a plaintiff has standing in a suit based on alleged deception and misstatements during a tender offer. Specifically, the *Crane* court decided whether a tender offeror has standing to sue under section 10(b) of the '34 Act and Rule 10b-5 to redress allegedly fraudulent practices occurring during a tender offer.

Crane Company (Crane) and American Standard, Inc., (Standard) were waging a takeover battle for control of Westinghouse Air Brake Company (Air Brake).[46] When Crane began purchasing Air Brake stock in 1967, Air Brake informed Crane of Air Brake's opposition to a merger

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[41] 435 F. Supp. at 1368. The Supreme Court construes strictly the purchaser-seller requirement of Rule 10b-5. *See* Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 731, 749 (1975). The Court stated that absent such a strict construction, courts would face a boundless class of non-purchasing or non-selling plaintiffs who would seek some type of relief for a Rule 10b-5 violation. *Id.* at 740. *Hundahl* correctly found that this concern is not present as to non-tendering shareholders under § 14(e) because the class of potential plaintiffs is limited to non-tendering holders of target company stock. *See* 465 F. Supp. at 1368.

[42] *See* note 33 *supra*.

[43] *See* 2 BROMBERG & LOWENFELS, SECURITIES FRAUD AND COMMODITIES FRAUD § 6.3 (1979) (Congress showed as much concern for non-tendering as for tendering shareholder by eliminating Rule 10b-5's purchase or sale requirement).

[44] *See* Piper v. Chris-Craft Indus., Inc., 430 U.S. at 38 (omission of purchaser-seller requirement may evidence congressional desire to protect shareholder-offerees who decide not to tender stock). The lower courts are in virtual agreement that a private cause of action exists under § 14(e) in favor of a non-tendering target shareholder. *See, e.g.*, Smallwood v. Pearl Brewing Co., 489 F.2d 579, 596 (5th Cir. 1974); Electronic Specialty Co. v. International Controls Corp., 409 F.2d 937, 946 (2d Cir. 1969); Hurwitz v. R.B. Jones Corp., 76 F.R.D. 149, 161 (W.D. Mo. 1977); McCloskey v. Epko Shoes, Inc., 391 F. Supp. 1279, 1282 (E.D. Pa. 1975); Petersen v. Federated Dev. Co., 387 F. Supp. 355, 359 (S.D.N.Y. 1974). *But see* Neuman v. Electronic Specialty Co., [1969-1970 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 92,591 at 98,703 (N.E. Ill. 1969) (if court does not restrict standing, non-tenderor could, subsequent to tender offer, file claim for damages resulting from his decision not to tender rather than from misdeeds of the defendant). *See generally*, ARANOW, EINHORN, & BERLSTEIN, *supra* note 2, at 115; Pitt, *supra* note 3, at 189-90; Note, *Standing to Sue Under Section 14(e)*, 26 KAN. L. REV. 624, 636 (1978).

[45] 603 F.2d 244 (2d Cir. 1979).

[46] *Id.* at 245.

with Crane.[47] After Crane continued making open market purchases of Air Brake stock, Air Brake raised the cumulative vote necessary to obtain representation on its board of directors.[48] Air Brake's directors also approved a merger of Air Brake into Standard to fend off Crane's takeover attempt.[49] Crane countered with an exchange offer of subordinated debentures for each share of Air Brake stock.[50] This tender offer, coupled with open market purchases, resulted in Crane owning 32.2 percent of Air Brake's outstanding stock on May 24, 1968.[51] The Air Brake stockholders, however, already had approved the merger of Air Brake into Standard at a May 16 stockholders' meeting.[52]

Crane filed suit under section 10(b)[53] and Rule 10b-5[54] alleging misrepresentations in Air Brake's proxy statement soliciting votes for the proposed merger, and fraud and market manipulation by Standard.[55] The Second Circuit, relying on *Chris-Craft*, which held that a tender offeror lacked standing under section 14(e) for alleged tender offer irregularities,[56] decided that a tender offeror lacks standing under Rule 10b-5 for alleged fraud in connection with a tender offer.[57]

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[47] *Id.*

[48] *Id.* A reluctant target company often increases the cumulative vote necessary to obtain representation on its board of directors as a defensive tactic to frustrate the takeover attempt. *See* LIPTON & STEINBERGER, *supra* note 2, § 6.2.2.

[49] 603 F.2d at 246. Prior to the approval of a merger of Air Brake into Standard, Crane filed statements with the SEC declaring an intention to solicit proxies for the election of Air Brake directors. *Id.* at 245-46.

[50] *Id.* at 246. Crane's exchange offer originally was open from April 10, 1968, through April 19, 1968. On April 19, Standard purchased a large block of Air Brake stock on the open market, thereby making the market activity with respect to Air Brake stock apparently increase. At the same time, Standard made two undisclosed, off-the-market sales of the same stock. *Id.* Crane alleged that this buying and selling of Air Brake stock by Standard violated § 10(b) and Rule 10b-5. *Id.; see* text accompanying note 55 *infra*. Crane extended its tender offer several times so that the final expiration date was May 24, 1968. 603 F.2d at 246.

[51] *Id.*

[52] *Id.* The merger of Air Brake into Standard became effective on June 7, 1968. As a result of the merger, Crane owned 740,211 shares of Standard convertible preferred stock. Under threat of an antitrust suit by Standard, a competitor of Crane's in the plumbing industry, Crane sold all but 10,000 of these shares. *See id.*

[53] 15 U.S.C. § 78j(b) (1976).

[54] 17 C.F.R. § 240.10b-5 (1979); *see* note 16 *supra*.

[55] 603 F.2d at 246. In addition to claiming violation of § 10(b) and Rule 10b-6, Crane alleged violations of § 9 and § 14 of the '34 Act, 15 U.S.C. §§ 78i, 78n (1976); Rule 10b-6, 17 C.F.R. § 240.10b-6 (1979); and Regulation 14a, 17 C.F.R. § 240.14a-1 *et seq.* (1979).

[56] *See* text accompanying notes 27-31 *supra*.

[57] 603 F.2d at 249. The district court dismissed Crane's original complaint because of lack of standing. *Id.* at 247. On appeal, the Second Circuit reversed in part, holding that Crane had standing to sue under §§ 9 & 10 of the '34 Act, 15 U.S.C. §§ 78i, 78j (1976). *See* Crane Co. v. Westinghouse Air Brake Co., 419 F.2d 787, 798 (2d Cir. 1969). The Second Circuit also held that Standard violated § 9 (a)(2) (one may not buy or sell a listed security to create artificial market activity), § 10(b), and Rule 10b-5. *Id.* at 795-98. Standard violated § 10(b) and Rule 10b-5 by failing to disclose the manipulation of Air Brake stock. *Id.; see* note 50 *supra*. The Second Circuit remanded the case to the district court for a determina-

The *Crane* court first noted that the language of Rule 10b-5 and section 14(e) is substantially identical.[58] Because section 14(e), however, deals specifically with tender offers, section 14(e) is the more appropriate basis for a defeated tender offeror's suit.[59] Since the Supreme Court held in *Chris-Craft* that a tender offeror's suit under section 14(e) is inappropriate, the *Crane* court was not willing to imply a cause of action for a defeated tender offeror under the more general provisions of Rule 10b-5.[60]

The *Crane* court examined the legislative history of section 10(b)[61] and concluded that section 10(b), like section 14(e),[62] was enacted to protect investors and not tender offerors.[63] *Crane* thus limited the right to bring a cause of action under section 10(b) and Rule 10b-5 to defrauded investors.[64] As an investor, Crane made a profit of approximately $10 million by selling the Standard shares received in the merger.[65] Therefore, Crane was not a defrauded investor and thus could sue only as a defeated tender offeror by claiming that Standard's actions illegally prevented Crane from acquiring control of Air Brake. The court held that Crane, suing as a defeated tender offeror, was not an intended beneficiary of section 10(b) and Rule 10b-5 and had no standing to bring suit.[66]

The court also enumerated certain policy considerations supporting the denial of standing to Crane. First, the threat of a damage suit by a

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tion of damages. 419 F.2d at 803.

Before the district court rendered a decision, the Supreme Court decided *Chris-Craft*. *See* text accompanying notes 27-31 *supra*. The district court then reconsidered whether Crane, as a tender offeror, had standing to bring suit under Rule 10b-5 and held that *Chris-Craft* precluded such standing. *See* Crane Co. v. American Standard, Inc., 439 F. Supp. 945, 951 (S.D.N.Y. 1977). The Second Circuit affirmed the post-*Chris-Craft* denial of standing. *See* 603 F.2d at 249-51.

Crane argued that the district court, in denying standing on remand, violated the "law of the case" doctrine. *See id.* at 248. The Second Circuit held that regardless of the propriety of the district court's decision, the Second Circuit was not bound by the previous decision. *Id.* Recognizing that the law of the case doctrine is not rigid, the court reconsidered the threshold question of standing since a denial of standing would avoid further proceedings on the merits and thus conserve judicial resources. *Id.* Such concern is ironic given that the *Crane* case was in litigation for 11 years.

[58] *Id.* at 249.

[59] *Id.*

[60] *Id.*

[61] Section 10(b) of the '34 Act, 15 U.S.C. § 78j(b) (1976), gives the SEC rulemaking authority with respect to fraud in connection with the purchase and sale of securities. The SEC promulgated Rule 10b-5 pursuant to this authority. *See* 603 F.2d at 249 n.11. Therefore, the scope of Rule 10b-5 and the authority to bring an action based on Rule 10b-5 violations cannot exceed the authority allowed under § 10(b). *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 212-14 (1975).

[62] *See* text accompanying note 29 *supra*.

[63] 603 F.2d at 250; *see* 78 CONG. REC. 2271 (1934) (section 10(b) forbids devices detrimental to proper protection of investors). *See also* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 198 (1976) (overall purpose of '33 and '34 Acts is to protect investors).

[64] 603 F.2d at 250.

[65] *Id.; see* note 52 *supra*.

[66] 603 F.2d at 250-51.

defeated tender offeror would provide little additional protection for investors.[67] Second, injunctive relief at an earlier stage of the proceeding is a more efficient remedy for illegal conduct than a damages suit which only provides retrospective relief.[68] Third, the former stockholders of Air Brake who allegedly were misled by Standard's actions were now, because of the merger, stockholders of Standard. Any liability imposed on Standard ultimately would fall on these shareholders. The Second Circuit reasoned that an anomalous situation would result if former stockholders of Air Brake, who allegedly were misled by Standard's actions, had to bear the cost of satisfying the damages allegedly suffered by Crane.[69]

In light of *Chris-Craft*, the *Crane* decision denying a defeated tender offeror standing to sue under Rule 10b-5 is sound. Section 14(e) of the '34 Act prohibits fraud in connection with tender offers. *Chris-Craft*, however, precludes a tender offeror from suing under section 14(e). Therefore, tender offerors should not be able to sue under the much broader provisions of section 10(b) and Rule 10b-5. Though *Crane* is the first decision after *Chris-Craft* to consider the standing of a defeated tender offeror under section 10(b) and Rule 10b-5, the *Crane* decision should provide strong precedential value. Adoption of the *Crane* rationale will effectuate the legislative intent behind section 10(b) and Rule 10b-5 while not affecting the rights of the investors who must decide whether or not to tender their shares. Thus, *Crane* and *Hundahl* both insure that the corporate investors, the intended beneficiaries of the anti-fraud provisions of the federal securities laws, can sue for misconduct during tender offers.

B. *Prohibited Tender Offer Practices*

Rule 10b-5[70] and section 14(e)[71] are anti-fraud provisions preventing

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[67] *Id.* at 250. The *Crane* court stated that the deterrent value of a possible suit by a defeated tender offeror is speculative since there already exists a potential class of plaintiffs, the investors, who are available to enforce the prohibitions of § 10(b) and Rule 10b-5. *Id.* Moreover, implying a cause of action in favor of Crane arguably could prejudice some investors by deterring tender offers because of the possibility of a massive damage claim against the tender offeror. *Id.*

[68] *Id.* at 251. Injunctive relief is a more efficient remedy for securities violations than damages because an injunction prevents the harm from ever occurring. In contrast, a suit for damages occurs only after the illegal conduct causes harm. A suit for damages thus seeks to undo harm that has already taken place. The court in *Crane* noted that Crane sought injunctive relief in 1968 to prevent the consummation of the merger. Upon denial of the injunction, Crane relied exclusively on the possibility of retrospective relief in a suit for damages. The Second Circuit stated that Crane had to bear the consequences of this choice of litigation strategy. *Id.*

[69] *Id.* The *Crane* court, in denying standing to Crane upon § 10(b) and Rule 10b-5, emphasized that § 14(e) did not confer important, new rights on a tender offeror. *Id.; see* Piper v. Chris-Craft Indus., Inc., 430 U.S. at 30. *Crane* held that the Supreme Court's characterizing a tender offeror's suit for damages as a new right in discussing § 14(e) implied that no such cause of action existed under prior federal law, which included § 10(b) and Rule 10b-5. 603 F.2d at 251.

[70] 17 C.F.R. § 240.10b-5 (1979); *see* note 16 *supra*.

manipulation and deception with respect to securities transactions. Neither provision, however, defines what constitutes a manipulative or deceptive practice. Therefore, the courts must determine the practices prohibited by Rule 10b-5 and section 14(e).

Hundahl v. United Benefit Life Insurance Co.[72] examined the relationship between a breach of a fiduciary duty[73] and a violation of Rule 10b-5 to determine whether a breach of such a duty is actionable under Rule 10b-5. Mutual of Omaha Insurance Company (Mutual) began acquiring shares of United Benefit Life Insurance Company (United) in 1951.[74] Thereafter, Mutual and various outside experts conducted studies to evaluate United's stock.[75] The Mutual Investment Committee appointed a special subcommittee to oversee the continued acquisition of United stock.[76] At each annual meeting from 1970 through 1977, the Mutual policyholders authorized the policyholders investment-executive committee to implement a program to acquire the shares of United and other subsidiaries.[77]

During the initial stages of Mutual's acquisition program, Mutual allocated joint operating expenses between the two companies according to a formula devised by Arthur Andersen & Co.[78] The Andersen formula allocated expenses according to the relative benefits derived by each company, except for advertising expenses which were borne by Mutual.[79] Mutual adopted a new plan in 1965 under which Mutual and United equally shared agency management expenses.[80] Further changes in the allocation

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[71] 15 U.S.C. § 78n(e) (1976); *see* note 15 *supra*.

[72] 465 F. Supp. 1349 (N.D. Tex. 1979). *See* text accompanying notes 19-44 *supra*.

[73] A fiduciary relationship exists between the controlling factions of a corporation and the corporation's minority stockholders. *See* United States v. Byrum, 408 U.S. 125, 137 (1972). Those owing a fiduciary duty must not exercise their corporate control in such a way as to promote personal interests to the detriment of the interests of the corporation and minority stockholders. *Id.*

[74] 465 F. Supp. at 1354. Mutual and United are both insurance companies incorporated and headquartered in Nebraska. *Id.* at 1353. United is a stockholder-owned life insurance company. *Id.* Mutual is a mutual legal reserve company engaged primarily in selling and underwriting health and accident insurance. *Id.* The two companies were jointly operated but not jointly owned. The National Association of Insurance Commissioners (NAIC) advised Mutual in 1949 to acquire all outstanding shares of United to alleviate the continuing conflict of interest risk caused by joint operation. *Id.* In 1951, Mutual sought a declaratory judgment from a Nebraska state court as to the legality of the proposed purchase of United shares. The legality of such a transaction was upheld provided that Mutual invested no more than 35% of its surplus in United stock. *Id.* at 1354.

[75] *Id.*

[76] *Id.* Mutual continually made open-market purchases of United stock during the 26 years preceding the 1977 tender offer. *Id.* Beginning in 1968, Mutual made these purchases through an intermediary because of fear that disclosure of the purchasing efforts might raise the price of United stock. *Id.*

[77] *Id.*

[78] *Id.* at 1354-55.

[79] *Id.* at 1355.

[80] *Id.*

formula resulted in United paying forty-nine percent of the advertising expenses in 1975, and incurring substantial portions of the start-up expenses of three new Mutual subsidiaries.[81]

After Mutual made a tender offer for United shares in October 1977,[82] shareholders of United filed suit alleging that Mutual, through its acquisition plan, attempted to downplay United's value, thereby depressing United's stock price to facilitate Mutual's takeover.[83] The elements of the alleged scheme to depress United's stock price included improper allocation of joint expenses to United, a low dividend policy for United, use of unreasonably conservative accounting procedures in the preparation of United's financial reports, and failure to disclose these procedures as well as the true value of United's assets.[84] Plaintiffs claimed that this scheme constituted manipulation and misrepresentation prohibited by section 10(b) and Rule 10b-5.[85]

The *Hundahl* court first examined the plaintiff's claims to determine whether the alleged conduct on the part of Mutual constituted manipulation[86] under Rule 10b-5.[87] The *Hundahl* plaintiffs argued that any breach

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[81] *Id.*

[82] *See* text accompanying note 21 *supra.*

[83] 465 F. Supp. at 1354.

[84] *Id.*

[85] *Id.* Plaintiffs in *Hundahl* also alleged certain violations of § 14(e). *Id.* at 1355-56. After holding that the non-tendering shareholders had standing to assert a § 14(e) claim, *see* text accompanying notes 19-44 *supra*, the *Hundahl* court did not reach the merits of the § 14(e) claim due to the holding on the reliance issue. *See* text accompanying notes 176-89 *infra.*

[86] Manipulation is a term of art that refers generally to practices intended to mislead investors by artificially affecting market activity. *See* Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 476 (1977); note 91 *infra.*

[87] 465 F. Supp. at 1359-63. Before reaching the merits of plaintiffs' Rule 10b-5 claims, the *Hundahl* court faced the question of whether one of the plaintiffs, who had neither purchased nor sold securities, had standing to seek injunctive relief under Rule 10b-5. The court held that such standing exists. *Id.* at 1357.

The Supreme Court strictly construed the purchaser-seller requirement in Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 731, 749 (1975), which involved a suit for money damages. *See* note 41 *supra. Hundahl* held that the *Blue Chip* reasoning does not preclude a Rule 10b-5 suit by a non-purchaser or non-seller for injunctive relief. *See* 465 F. Supp. at 1358-59. The *Hundahl* court first noted that one who neither purchases nor sells a security seeks a conjectural and speculative monetary award because there is no precise number of shares on which to calculate a damage award. Tabulation of the precise number of shares involved is not necessary when injunctive relief is sought because there is no need to calculate any damage award. *Id.* at 1358. Moreover, the proof in a damage suit involving one who neither purchases nor sells securities rests largely on uncorroborated testimony. A plaintiff in such suit must prove what he would have done had the defendant not engaged in the allegedly unlawful conduct. Plaintiff's testimony would amount to little more than speculation. In a suit for injunctive relief, however, a plaintiff must prove a specific injury. A suit for injunctive relief will thus not rest on wholly subjective evidence. *Id.*

Finally, there is no danger of creating an infinite class of potential plaintiffs by allowing a suit by a non-purchaser or non-seller for injunctive relief under Rule 10b-5. Past purchasers of United stock who are presently minority shareholders are easily identified. Hence, the possibility of vexatious litigation pursued for settlement value alone is minimized. *Id.* at

of fiduciary duty coupled with an intent to affect market prices constitutes manipulation.[88] The defendants[89] countered that intent alone is not enough and that only activities in the marketplace can constitute manipulation under Rule 10b-5.[90] Based largely on the Supreme Court's holding in *Santa Fe Industries, Inc. v. Green*,[91] the *Hundahl* court found for the defendants and dismissed the Rule 10b-5 claims of manipulation.[92]

The *Hundahl* court began its analysis by examining the common law decisions involving manipulation.[93] Courts, before the enactment of the federal securities laws, held that the securities market requires market freedom to function properly and that any scheme that interferes with that free market mechanism is manipulative.[94] These manipulative schemes, according to the *Hundahl* court, invariably involved marketplace transactions that artificially affected the market price of a listed stock.[95] The court then held that the '34 Act did not expand the common law view of manipulation.[96] In *Santa Fe*, the Supreme Court cited section 9 of the '34 Act as indicative of the type of activities encompassed under the term "manipulation."[97] Section 9 prohibits "manipulation of security prices" by proscribing conduct involving marketplace activity that artifi-

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1358-59; *accord*, Fuchs v. Swanton Corp., M.P.C. [Current] FED. SEC. L. REP. (CCH) ¶ 97,133 at 96,249-50 (S.D.N.Y. Sept. 28, 1979). *But see* Initio, Inc. v. Hesse, 474 F. Supp. 312, 320 (D. Del. 1979); Krueger v. Kirkpatrick, 466 F. Supp. 800, 805-06 (D. Neb. 1979).

[88] 465 F. Supp. at 1359.

[89] The defendants in *Mutual* included Mutual, the chief executive officer and chairman of the board of directors of both Mutual and United, the president and chief operating officer of Mutual, the senior executive vice president of Mutual and United, United (for derivative purposes only), and the vice-chairman of Mutual's board of directors. *Id.* at 1353.

[90] *Id.* at 1359.

[91] 430 U.S. 462 (1977). Santa Fe Industries, Inc. (Santa Fe) owned 95% of the stock of Kirby Lumber Corp. (Kirby). *Id.* at 465. Santa Fe could thus take advantage of Delaware's "short-form merger" statute which allows a parent corporation, owning at least 90% of the stock of a subsidiary, to merge with that subsidiary upon approval by the parent's board of directors. *See* DEL. CODE tit. 8, § 253 (1975). The statute does not require advance notice to or approval of minority stockholders with respect to the merger. *Id.* Minority shareholders of Kirby sued alleging that the offered price for their shares in the merger was inadequate, that Santa Fe knew that the appraised value of Kirby stock was fraudulent, and that Santa Fe offered a premium over the appraised value to convey a false impression of generosity. 430 U.S. at 467. Plaintiffs claimed that this conduct violated Rule 10b-5. *Id.* at 467-68. The Supreme Court disagreed holding that the alleged conduct did not constitute manipulation or deception within the meaning of Rule 10b-5. *Id.* at 474.

[92] 465 F. Supp. at 1359-63.

[93] *Id.* at 1360-61.

[94] *See, e.g.*, United States v. Brown, 5 F. Supp. 81, 85 (S.D.N.Y. 1933), *aff'd on other grounds*, 79 F.2d 321 (2d Cir.), *cert. denied sub nom.* McCarthy v. United States, 296 U.S. 650 (1935) (one reading a price quotation on a stock exchange is justified in believing that quoted price is result of series of sales between parties dealing at arms length in free and open market). *See also* Harris v. United States, 48 F.2d 771 (9th Cir. 1931); Sampson v. Shaw, 101 Mass. 145 (1809).

[95] 435 F. Supp. at 1360-61.

[96] *Id.* at 1361.

[97] Santa Fe Indus., Inc. v. Green, 430 U.S. at 476.

cially affects the price of a stock.[98] Since all the manipulative devices prohibited by section 9 give the false impression that market activity is occurring due to supply and demand forces, *Hundahl* held that Rule 10b-5 prohibits the same type of manipulative conduct.[99] This construction of the scope of Rule 10b-5 excludes conduct not occurring in the marketplace.

In holding that the defendants' activities did not amount to manipulation, the *Hundahl* court also was sensitive to several policy considerations.[100] Recent Supreme Court decisions limit the scope of federal securities law so not to infringe on the province of state courts.[101] The plaintiffs' claim in *Hundahl* was basically a state law claim for breach of a fiduciary duty.[102] Allowing the *Hundahl* plaintiffs to bring this type of claim could result in a boundless class of plaintiffs who would couple allegations of corporate unfairness and intentional manipulation of the market price of a stock to gain access to federal court.[103]

In examining the Supreme Court's decision in *Santa Fe*, the common law decisions involving securities manipulation, the legislative history of the '34 Act, and certain policy considerations, the *Hundahl* court formulated a definition of manipulation that includes only practices in the marketplace which create the false impression that certain market activity is ocurring and which tamper with the price of a stock.[104] The defendants in *Hundahl* engaged in no market activity. At most, the *Hundahl* defendants only had an intent to manipulate the market price. Such manipulative intent is merely a breach of a fiduciary duty and is not the type of conduct encompassed by the Rule 10b-5 definition of manipulation.[105]

The *Hundahl* court stated that the narrow definition of manipulation under Rule 10b-5 is not overly restrictive because few attempts to affect the market price of stock artificially could succeed without being actiona-

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[98] *See* 15 U.S.C. § 78i (1976). Specifically, § 9 prevents such practices as rigged prices, fictitious or "wash" sales, and matched orders for the purpose of creating an inaccurate picture of market activity. *See* 15 U.S.C. §§ 78i(a)(6), (1) (1976).

[99] 435 F. Supp. at 1361-62. The *Hundahl* court did not address whether the scope of § 10b and the scope of § 9 are coextensive. *Id.* at 1361. The court did hold that the legislative history of the '34 Act supports the conclusion that § 9 and Rule 10b-5 proscribe the same type of activity. *Id.* at 1361-62. *See also* S. REP. No. 792, 73d Cong., 2d Sess. (1934).

[100] 435 F. Supp. at 1362-63.

[101] *See, e.g.*, Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 474 (1977) (mere breach of fiduciary duty not violation of Rule 10b-5); Piper v. Chris-Craft Indus., Inc., 430 U.S. 1, 42 (1977) (defeated tender offeror lacks standing to sue under § 14(e)); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 749 (1975) (strict construction of Rule 10b-5's purchaser-seller requirement).

[102] 435 F. Supp. at 1362. *See* note 73 *supra.*

[103] *Id.* at 1362-63.

[104] *Id.* at 1360.

[105] *See* Santa Fe Indus., Inc. v. Green, 430 U.S. at 477 (mere corporate mismanagement not within prohibitions of Rule 10b-5). *See generally* Sherrard, *Federal Judicial and Regulatory Responses to* Santa Fe Industries v. Green, 35 WASH. & LEE L. REV. 695, 696-97 (1978); Note, *Section 10(b)—The Manipulation and Deception Requirement*, 52 IND. L. REV. 641, 644 (1978).

ble as deception under Rule 10b-5.[106] Rule 10b-5 imposes an affirmative duty to disclose material facts.[107] Once material facts are disclosed, however, no duty exists to explain the significance of the information.[108] A plaintiff cannot "bootstrap" his way into federal court by alleging state law violations[109] and then claiming that the defendant failed to disclose violations of state law.[110]

The majority of the *Hundahl* plaintiffs' claims of deception were not actionable[111] because the plaintiffs alleged a failure to explain disclosed facts.[112] The only arguable deceptive act cognizable under federal law was the defendants' failure to disclose that a dividend restriction, implemented over ten years earlier but still in effect, was no longer valid.[113] Moreover, all the claims of deception failed to amount to actionable conduct under Rule 10b-5.[114] The *Hundahl* court rightfully recognized that the line between mismanagement and non-disclosure is one that cannot be drawn with precision.[115] The court adhered closely to the spirit of *Santa Fe* and held that when the "central thrust," of a claim arises from corporate mismanagement, the claim is not actionable under federal

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[106] 435 F. Supp. at 1362.

[107] *See* 17 C.F.R. § 240.10b-5 (1979); note 16 *supra.*

[108] 435 F.Supp. at 1364; *see* note 110 *infra.*

[109] The state law violations which traditionally form the basis of the "bootstrap" argument are violations of fiduciary duties. *See* note 73 *supra.*

[110] 435 F. Supp. at 1364; *see* Golub v. PPD Corp., 576 F.2d 759, 765 (8th Cir. 1978) (defendants have no duty to characterize motivation for their conduct); Popkin v. Bishop, 464 F.2d 714, 719-20 (2d Cir. 1972) (defendants have no duty to comment on wisdom or fairness of particular conduct because Rule 10b-5 imposes a duty to disclose and inform rather than to pass judgment); Goldberger v. Baker, 442 F. Supp. 659, 664 (S.D.N.Y. 1977) (even under narrowest reading of *Santa Fe*, deception requires allegation of more than mere failure to disclose the unfairness of a transaction); Spielman v. General Host Corp., 402 F. Supp. 190, 206 (S.D.N.Y. 1975) (investors must be completely informed as to material matters but no requirement that adequately disclosed information be "spoonfed"); Stedman v. Storer, 308 F. Supp. 881, 887 (S.D.N.Y. 1969) (securities laws were never meant to require psychoanalysis or self-analysis); Carliner v. Fair Lanes, Inc., 244 F. Supp. 25, 29 (D. Md. 1965) (improper purpose and failure to disclose that purpose does not violate Rule 10b-5).

[111] 435 F. Supp. at 1365. The plaintiffs in *Hundahl* alleged several instances of deception. These allegations included failure to disclose a breach of fiduciary duty, to reveal mismanagement, to state that the allocation of expenses was unfair to United, to disclose the concealment of United's true profitability, and to state that the financial reports of United did not reflect the company's true value. *Id.* at 1365-66. The court held none of these claims actionable under Rule 10b-5 since the defendants did not conceal facts. *Id.* at 1364-65. The defendants merely failed to label and pass judgment on disclosed information. *Id.*

[112] *Id.*

[113] A dividend restriction, stemming from a recommendation of the NAIC, was in effect since 1954-55. Defendants disclosed the restriction but not the fact that the NAIC would lift the restriction upon request. *Id.* at 1365. Although the *Hundahl* court recognized that the claim was analogous to one for mismanagement for failure to request the lifting of the restriction, the court stated that a question of fact existed as to whether the claim is cognizable under Rule 10b-5. *Id.* Therefore, the court did not dismiss this claim. *Id.*

[114] 435 F. Supp. at 1365.

[115] *Id.* at 1364.

law.[116]

The rule announced by the *Hundahl* court is not difficult conceptually. Claims based on breaches of fiduciary duty are not within the scope of the federal securities laws. A precise line between mismanagement and non-disclosure, however, cannot be drawn. The practical result is that courts possess the flexibility to take an expansive or restrictive view of federal securities law. The *Hundahl* approach is an example of a fairly strict reading of the federal law.[117] *Lewis v. McGraw-Hill, Inc.*[118] exemplifies the more liberal approach to the scope of federal securities law.

On January 8, 1979, American Express Company (AMEXCO) publicly proposed a friendly business combination to McGraw-Hill, Inc. (McGraw-Hill).[119] The directors of McGraw-Hill rejected the proposed offer.[120] Shareholders of McGraw-Hill then sued the McGraw-Hill directors for violations of section 14(e).[121] Specifically, the plaintiffs alleged that the defendants announced that AMEXCO's proposed offer price was inadequate knowing that the proposal was fair, unlawfully publicly challenged the integrity of AMEXCO and the legality of the proposed tender offer, published a letter that McGraw-Hill sent AMEXCO characterizing the proposed tender offer as "reckless," "illegal," and "improper," and failed to disclose that McGraw-Hill previously told AMEXCO that McGraw-Hill considered AMEXCO to be a desirable merger partner.[122] The plaintiffs thus argued that the tender offer would have been successful but for defendants' conduct which allegedly violated statutory and common law fiduciary duties.[123]

Before deciding whether the plaintiffs' allegations were actionable under section 14(e), the *Lewis* court held that section 14(e) prevents manipulative and deceptive practices when an offeror merely "proposes" a tender offer.[124] The court emphasized that section 14(e) operates "in connection with any tender offer."[125] Conduct prior to the actual making of a tender offer can have as pervasive an influence on the target shareholders

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[116] *Id.* at 1365-66.

[117] The *Hundahl* court justified its restrictive view of the federal securities law by relying on Supreme Court decisions which indicate that the Court is restricting the scope of these laws. *See id.* at 1362-63; *see, e.g.*, Santa Fe Indus., Inc. v. Green, 430 U.S. 462 (1977) (actionable conduct); Piper v. Chris-Craft Indus., Inc., 430 U.S. 1 (1977) (standing under § 14(e)). Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975) (standing under Rule 10b-5).

[118] [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 (S.D.N.Y. Nov. 30, 1979).

[119] *Id.* at 96,567. The basis of the friendly business combination proposed by American Express Company (AMEXCO) was AMEXCO's ownership of 49 per cent of the outstanding securities of McGraw-Hill. *Id.*

[120] *Id.*

[121] *Id. See* 15 U.S.C. § 78m(e) (1976); note 15 *supra.*

[122] [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 at 96,567, 96,569.

[123] *Id.* at 96,567.

[124] *Id.* at 96,568.

[125] *Id. See* 15 U.S.C. § 78m(e) (1976); note 15 *supra.*

as conduct after the formal announcement of the tender offer.[126] If section 14(e) does not apply to conduct prior to the formal announcement of a tender offer, a party could make omissions and misstatements until the formal offer without fear of legal reprise.[127] These omissions and misstatements easily could influence the future decision of target stockholders on whether to tender their shares.[128] Hence, once a public announcement of a proposed tender offer establishes a clear and definite intent to make a tender offer, the prohibitions of section 14(e) apply.[129] The *Lewis* court's holding that section 14(e) covers proposed tender offers furthers the congressional intent of protecting the target shareholder who ultimately must decide whether or not to tender.[130]

Once the *Lewis* court decided that section 14(e) applies to proposed tender offers, the court addressed the alleged violation of that section. The *Lewis* defendants argued that the plaintiffs simply alleged breaches of corporate fiduciary duty which do not constitute deception under section 14(e) in light of *Santa Fe*.[131] The *Lewis* court responded that *Santa Fe* does not ban all claims based on breaches of state law fiduciary duty under section 14(e).[132] According to the court, *Santa Fe* requires only an allegation of non-disclosure or misleading disclosure.[133] The court held that while plaintiffs' allegations involved breaches of fiduciary duties, the allegations also involved non-disclosure and misleading disclosure, and thus stated a cause of action for deception under section 14(e).[134]

Although seemingly contradictory, the *Hundahl* and *Lewis* decisions are distinguishable. Unlike the *Lewis* plaintiffs, the plaintiffs in *Hundahl* did not allege statements or omissions designed to mislead the target corporation's shareholders.[135] Both cases, however, basically involved claims

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[126] [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 at 96,568 (quoting Applied Digital Data Systems, Inc. v. Milgo Elec. Corp., 425 F. Supp. 1145, 1154 (S.D.N.Y. 1977)).

[127] *Id.*

[128] *Id.*

[129] [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 at 96,568. *See also* Reserve Management Corp. v. Anchor Daily Income Fund, Inc., 459 F. Supp. 597, 608 (S.D.N.Y. 1978) (§ 14(e) applies when there is public announcement of clear and definite intent to make tender offer); Applied Digital Data Systems, Inc. v. Milgo Elec. Corp., 425 F. Supp. 1145, 1153-55 (S.D.N.Y. 1977) (failure to apply § 14(e) to proposed tender offers frustrates remedial purposes of statute); ARANOW & EINHORN, *supra* note 3, at 122-25; LIPTON & STEINBERGER, *supra* note 2, § 2.3.7; Note, *1976-1977 Securities Law Developments: Tender Offers*, 34 WASH. & LEE L. REV. 945, 946-54 (1977). *Cf.* ICM Realty v. Cabot, Cabot & Forbes Land Trust, 378 F. Supp. 918 (S.D.N.Y. 1974) (court allows § 14(e) suit during proposed tender offer period).

[130] *See* 113 CONG. REC. 854, 24664 (1967); note 33 *supra*. *Lewis* held that § 14(e) applies to proposed tender offers in a suit for injunctive relief or damages. [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 at 96,568.

[131] *Id.* at 96,569. *See* note 92 *supra*.

[132] [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 at 96,569.

[133] *Id.*

[134] *Id.; accord*, Houlihan v. Anderson-Stokes, Inc., 434 F. Supp. 1330, 1335 (D.D.C. 1977).

[135] The plaintiffs in *Hundahl* did not allege any statements by the defendants that were

of non-disclosure of information that a target shareholder should have in deciding whether to tender his shares. The difference between the two decisions rests on differing philosophies concerning the scope of the anti-fraud provisions of the federal securities law.[136] The *Lewis* court's broad interpretation of the scope of section 14(e), however, is not without limits as shown by the decision in *In re Sunshine Mining Company Securities Litigation.*[137]

On March 19, 1977, Great Western United Corporation (Great Western) informed the Sunshine Mining Company (Sunshine Mining) of Great Western's intention to make a tender offer for Sunshine Mining stock at $16.25 a share if the Sunshine Mining board of directors approved the offer within twenty-four hours.[138] Absent such approval, Great Western informed Sunshine Mining that the offer would proceed, but at a lower price.[139] The Sunshine Mining board of directors did not give their approval.[140] Great Western made a public tender offer on March 23, 1977, an amended offer on September 19, and a final offer on October 4.[141] During this entire period, Sunshine Mining management made no public statements except to disclose the various developments with respect to the tender offer.[142] Sunshine Mining's board made no recommendation that the Sunshine Mining stockholders refrain from tendering their shares.[143]

Stockholders of Sunshine Mining sued Sunshine Mining's directors for violating section 14(e).[144] The complaint alleged that the directors of Sunshine Mining acted for their own selfish interests in complete disregard of their fiduciary duties by refusing and resisting Great Western's tender offer.[145] Plaintiffs claimed that such action by Sunshine Mining's directors constituted deception under section 14(e).[146]

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misleading. *See* text accompanying notes 82-84 *supra*. The *Hundahl* plaintiffs alleged a failure to explain adequately disclosed information. *Id.* In contrast, the *Lewis* plaintiffs alleged statements made by the defendants which, standing alone, were blatantly misleading. *See* text accompanying note 122 *supra*.

[136] The expansive reading of § 14(e) taken by the *Lewis* court was of little benefit to the *Lewis* plaintiffs due to the court's holding on the reliance requirement. *See* text accompanying notes 194-97 *infra*.

[137] [Current] FED. SEC. L. REP. (CCH) ¶ 97,217 (S.D.N.Y. June 4, 1979).

[138] *Id.* at 96,634.

[139] *Id.*

[140] *Id.*

[141] *Id.* On March 23, 1977, Great Western filed statements with Idaho state officials and with the SEC indicating that the tender offer was for 2,000,000 Sunshine Mining shares at $15.75 a share. Idaho officials claimed inadequacies in the filing and took steps to prevent the tender offer. Great Western filed suit challenging the constitutionality of the Idaho filing statute. *Id.* Great Western's suit resulted in an injunction preventing the State of Idaho from interfering in Great Western's takeover attempt. *Id.*

[142] *Id.*

[143] *Id.*

[144] *Id.*

[145] *Id.* at 96,635.

[146] *Id.*

The *Sunshine Mining* court held that even if all the allegations were true, the plaintiffs failed to state a cause of action cognizable under section 14(e).[147] Recognizing that the '34 Act is basically a disclosure act, the court stated that there was no deception in the alleged facts because Sunshine Mining's directors disclosed all material information.[148] Further, there was no manipulation because Sunshine Mining engaged in no market activity.[149] Although the plaintiffs arguably stated a cause of action under state law for breach of fiduciary duty, they failed to state a cause of action under the federal securities laws.[150]

The *Lewis* and *Sunshine Mining* decisions demonstrate a consistent philosophy regarding the federal securities laws. *Lewis* involved numerous allegations of non-disclosure and misleading disclosure[151] that were sufficient to state a cause of action under Rule 10b-5 or section 14(e) under the Southern District of New York's interpretation of *Santa Fe*.[152] Plaintiffs in *Sunshine Mining* did not allege either non-disclosure or misleading disclosure.[153] The mere allegation of breach of fiduciary duty is not actionable under the federal securities laws even under the most expansive reading of *Santa Fe*.[154]

Unlike *Lewis* and *Sunshine Mining*, the court in *In re Commonwealth Oil/Tesoro Petroleum Corporation Securities Litigation*[155] examined alleged conduct clearly amounting to more than a breach of fiduciary duty. On April 18, 1975, Tesoro Petroleum Corporation (Tesoro) made a tender offer for shares of Commonwealth Oil Refining Company (Corco).[156] The president and chief executive officer of Corco responded by publishing two full-page letters in the *Wall Street Journal* urging rejection of the

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[147] *Id.* at 96,635-36.

[148] *Id.*

[149] *Id. See* text accompanying notes 86-103 *supra.*

[150] [Current] FED. SEC. L. REP. (CCH) ¶ 97,217 at 96,635-36. On November 20, 1979, the SEC adopted Rule 14e-2. *See* SEC Securities Exchange Act Release No. 34-16384 (Nov. 20, 1979), 531 SEC. REG. & L. REP. (BNA) E-1 (1979). Rule 14e-2 requires the target company to publish or send or give to security holders a statement disclosing the company's position with respect to the tender offer within ten business days after the formal tender offer. The position statement must either recommend acceptance of the tender offer, express no opinion and state that the target company will remain neutral, or state that the target company is unable to take a position with respect to the tender offer. Further, the target company must state reasons for its position. *Id.* Thus, if this rule had been in effect at the time of Great Western's tender offer for Sunshine Mining stock, Sunshine Mining's failure to respond to the tender offer would violate the federal securities laws. The *Sunshine Mining* court's analysis under § 14(e), however, remains valid even in light of the adoption of Rule 14e-2.

[151] *See* text accompanying note 122 *supra.*

[152] *See* text accompanying notes 118-34 *supra.*

[153] *See* text accompanying notes 144-46 *supra.*

[154] *See* Santa Fe Indus., Inc. v. Green, 430 U.S. at 479-80.

[155] 467 F. Supp. 227 (W.D. Tex. 1979).

[156] *Id.* at 234. Tesoro's tender offer was for 5.5 million shares of Corco stock at $11.50 a share. *Id.*

tender offer.[157] Tesoro increased the tender offer price per share and Corco's opposition to the tender offer ceased.[158] The two companies then issued a joint press release stating that upon completion of the tender offer the companies would use their best efforts to develop a fair and equitable consolidation plan.[159] Upon successful completion of the tender offer, however, Corco had been, and still was, in financial trouble.[160] Tesoro suspended plans for consolidation[161] and Corco filed a petition for voluntary bankruptcy on March 2, 1978.[162]

Past and present stockholders of Corco sued alleging violations of section 14(e).[163] The plaintiffs claimed that the published letters were deceptive because they contained false representations made intentionally or with reckless disregard for the truth.[164] The plaintiffs further claimed that Tesoro and Corco's joint press release was deceptive because the release did not disclose an alleged agreement concerning future employment between Tesoro and the chief executive officer of Corco.[165] Plaintiffs also claimed that the joint press release was deceptive because the two companies made representations about future consolidation plans when Tesoro lacked sufficient knowledge of Corco and its financial structure to make such representations.[166] The court held each of these claims actionable under section 14(e).[167] The holding in *Commonwealth Oil* is correct since the claims alleged material omissions and misrepresentations, con-

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[157] *Id.* The first of the letters urging rejection of the tender offer was in the April 22, 1975 *Wall Street Journal. Id.* The letter expressed confidence in Corco's long-term prospects and stated that the tender offer failed to reflect adquately Corco's true value. *Id.* The second letter, published on April 28, contained the same basic representations and added that Corco's prospects "never looked brighter." *Id.*

[158] *Id.* The price Tesoro offered for each share of Corco's stock increased from $11.50 per share to $14.25 per share. *Id.*

[159] *Id.*

[160] *Id.* at 234-35. Tesoro successfully completed the tender offer on June 6, 1975. *Id.* at 235.

[161] *Id.* at 235. Tesoro issued a press release on October 22, 1976, announcing a suspension of plans for consolidation of Tesoro and Corco until Corco could demonstrate financial viability. *Id.*

[162] *Id.*

[163] *Id.* at 235-36, 240.

[164] *Id.* at 240.

[165] *Id.* at 243.

[166] *Id.*

[167] *Id.* at 240-48. Defendants in *Commonwealth Oil* contended that the plaintiffs lacked standing to bring claims based on § 14(e) because they were non-tendering shareholders. *Id.* at 241. The court held that non-tenderors had sufficient standing. *Id.* at 241-43; *see* text accompanying notes 15-44 *supra*. Defendants also contended that there could be no reliance on the alleged misrepresentations because the plaintiff-shareholders did not tender their shares. *See* note 189 *infra*.

The *Commonwealth Oil* defendants also argued immateriality as a matter of law as to the alleged misrepresentations in the joint press release. 467 F. Supp. at 244; *see* text accompanying note 159 *supra*. The court disagreed and held that the alleged agreement between Tesoro and Corco's chief executive officer of the alleged unfeasibility of consolidation could influence the reasonable investor. 467 F. Supp. at 244-45.

duct clearly prohibited by section 14(e).[168]

The *Commonwealth Oil* plaintiffs also alleged a violation of Rule 10b-5,[169] claiming that Tesoro knew that the letters in the *Wall Street Journal*[170] contained misstatements which Tesoro failed to correct.[171] The court held that this alleged conduct on the part of Tesoro did not violate Rule 10b-5 because there is no liability for non-disclosure unless there is some duty to disclose, and one party to a tender offer has no duty to correct misstatements by another party.[172] Moreover, Tesoro was unaware of the falsity of the statements when the *Wall Street Journal* published the letters.[173]

Commonwealth Oil's holding that Tesoro did not violate Rule 10b-5 by failing to correct the misstatements in the letters in the *Wall Street Journal* probably is correct. A party making a misleading misrepresentation should not be able to shift liability to another party because the latter had the opportunity to correct the misrepresentation several months after publication and failed to do so. Rule 10b-5 imposes no duty to correct misstatements on one who is neither the source nor the subject of the misstatement nor is aware of the misstatement when made.[174]

A review of the *Hundahl, Lewis, Sunshine Mining,* and *Commonwealth Oil* decisions emphasizes the tension between federal and state control of corporate misconduct. *Hundahl* illustrates a restrictive view of the scope of federal law while *Lewis,* even as limited by *Sunshine Mining,* represents a more expansive view of the federal securities laws. *Commonwealth Oil* is the only case that clearly falls under the ambit of federal law. Each court responds to the tension between federal and state control by drawing fine lines between corporate mismanagement amounting to a mere breach of fiduciary duty and conduct actionable under the antifraud provisions of the federal securities laws. The difficulty for the practicing attorney, however, lies in the fact that the lines between state and federal authority are not drawn in a consistent and predictable manner.

C. *Reliance Requirement for a Non-Tendering Shareholder*

Hundahl v. United Benefit Life Insurance Co.[175] and *Lewis v. McGraw-Hill*[176] upheld the standing of non-tendering shareholders to bring

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[168] *See* 15 U.S.C. § 78n(e) (1976); note 15 *supra.*

[169] 17 C.F.R. § 240.10b-5 (1979); *see* note 16 *supra.*

[170] *See* text acompanying note 157 *supra.*

[171] 467 F. Supp. at 239.

[172] *Id.* at 239-40; *accord,* Electronic Specialty Co. v. International Controls Corp., 409 F.2d 937, 949 (2d Cir. 1969) (company may choose to correct another's misstatements in press but nothing in federal securities law so requires).

[173] 467 F. Supp. at 240.

[174] *Id.*

[175] 465 F. Supp. 1349 (N.D. Tex. 1979); *see* text accompanying notes 21-44, 72-116 *supra.*

[176] [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 (S.D.N.Y. Nov. 30, 1979); *see* text accompanying notes 118-34 *supra.*

a private cause of action under section 14(e).[177] The defendants in each case then argued that the plaintiff-shareholders did not rely on a material omission or misrepresentation because the plaintiffs did not tender their shares.[178] The alleged fraudulent conduct arguably could not be the cause of any injury because the plaintiffs did not tender their shares and thus were not fraudulently deprived of the value of their investment.[179]

The *Hundahl* court stated that the purpose of the Williams Act is to insure full disclosure of all information to shareholders who must decide whether to accept a tender offer.[180] Thus, according to the court, the Williams Act protects shareholders who are misled by material omissions or misrepresentations in the course of a tender offer.[181] The plaintiffs in *Hundahl* were aware that the representations made by Mutual of Omaha Life Insurance Company[182] were untrue and thus were not misled into tendering their shares.[183] Since they were not misled, the plaintiffs were not the type of victims of non-disclosure that the Williams Act protects and, therefore, lacked standing[184] under section 14(e).[185]

The *Hundahl* decision to dismiss the plaintiffs' claims under section

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[177] *See* 15 U.S.C. § 78n(e) (1976); note 15 *supra*. *See generally* text accompanying notes 21-44 *supra*.

[178] *See* 465 F. Supp. at 1368-70; [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 at 96,570.

[179] *Id.*

[180] 465 F. Supp. at 1369.

[181] *Id.*

[182] *See* text accompanying note 84 *supra*.

[183] 465 F. Supp. at 1369.

[184] The *Hundahl* court stated that the plaintiffs lacked "standing" to sue because they were not misled by the allegedly fraudulent representations. *Id.* Such terminology is confusing since the court previously extended standing to the same plaintiffs as non-tendering shareholders. *Id.* at 1366-68. Perhaps the plaintiffs had standing to bring suit but the court dismissed their claims because the plaintiffs were unable to show injury recoverable under the Williams Act.

[185] 465 F. Supp. at 1369. The *Hundahl* court refused to state what the holding would be had the plaintiffs' reliance been at least an objective possibility. *Id.* The court stated, though, that a person who clearly did not rely on alleged misstatements could not recover. *Id.; see* St. Louis Union Trust Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 562 F.2d 1040, 1049 (8th Cir. 1977) (no recovery absent reliance).

The *Hundahl* court also examined the reliance issue from the vantage point of alleged injury. 465 F. Supp. at 1369-70. The plaintiffs claimed that Mutual's misrepresentations resulted in a successful tender offer which significantly decreased the value of the United shares. *Id.* at 1369. The court responded that the Williams Act prevents direct injuries resulting from the tendering or non-tendering of shares and that the plaintiffs' alleged injury was too attenuated to be recoverable under § 14(e). *Id.* at 1370. The court further stated that the measure of damage under § 14(e) is the difference between the offered price for the shares and their genuine value. *Id.* at 1369. Diminution in market value of a stock, the plaintiffs' alleged injury, is thus not part of the damage formula under § 14(e). *Id.* at 1369-70.

The *Hundahl* court further stated that allowing a recovery by non-tendering plaintiffs was unnecessary to effectuate the congressional goals of the Williams Act. *Id.* at 1370. Shareholders who actually relied on the misrepresentations could bring suit. *Id.* Hence, an expansion of the class of potential plaintiffs to include those who did not rely is unwarranted. *Id.*

14(e) is unsound. The approach taken by the *Hundahl* court indicates that a non-tendering shareholder, claiming misrepresentation by a tender offeror, must rely on the misrepresentation in deciding not to tender. A tender offeror's representations, however, will be made with the intent of inducing the shareholder to tender.[186] In effect, the *Hundahl* holding implies a purchaser-seller requirement under section 14(e).[187] This decision is incorrect because Congress specifically omitted such a requirement in enacting section 14(e) to give standing to those who do not qualify under Rule 10b-5.[188] The decision in *Hundahl* makes the distinction between section 14(e) and Rule 10b-5 meaningless.[189]

Other courts have not taken the restrictive view of reliance adhered to by the *Hundahl* court. The court in *McCloskey v. Epko Shoes, Inc.*[190] held that a non-tendering shareholder can have the value of his holdings seriously impaired by misrepresentations made by the tender offeror.[191] To require personal reliance by the non-tendering shareholder, according to the *McCloskey* court, implies a section 14(e) purchaser-seller requirement that Congress intended to eliminate.[192] The court stated that the reliance of those shareholders who do tender on a material misrepresentation is sufficient causation for a non-tendering shareholder.[193] The *McCloskey* analysis is correct and the refusal of the *Hundahl* court to adopt the *McCloskey* rationale results in a non-tendering shareholder lacking a remedy for injury caused by a tender offeror's misrepresentation.

In contrast to *Hundahl*, the refusal of the court in *Lewis v. McGraw-Hill*[194] to adopt a liberal reliance requirement is consistent with the Williams Act. Determining that section 14(e) applies when a tender offeror announces a clear and definite intent to make a tender offer, the *Lewis* court then held that since no tender offer was ever made, the plaintiffs

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[186] *But see In re* Commonwealth Oil/Tesoro Petroleum Corp. Sec. Litigation, 467 F. Supp. at 243-44 (alleged misrepresentation by tender offeror caused shareholders not to tender).

[187] *See* text accompanying notes 38-41 *supra.*

[188] *See* Piper v. Chris-Craft Indus., Inc., 430 U.S. at 38; text accompanying notes 38-41 *supra.*

[189] The restrictive view of reliance taken by the *Hundahl* court arguably will be available in a § 14(e) claim against the target company's management. Any misrepresentations by such a defendant will be made to induce a target shareholder not to tender. A shareholder could thus use the *Hundahl* analysis and argue reliance on the misrepresentation in deciding not to tender. *See In re* Commonwealth Oil/Tesoro Petroleum Corp. Sec. Litigation, 467 F. Supp. at 243 (reliance on target management's alleged misrepresentations caused non-tender).

[190] 391 F. Supp. 1279 (E.D. Pa. 1975).

[191] *Id.* at 1282. The injury suffered by non-tendering shareholders is a decline in the market value of retained stock. 465 F. Supp. at 1349; *see* Clayton v. Skelly Oil Co., [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,269 at 92,747 (S.D.N.Y. Dec. 30, 1977) (where deception adversely affects market for a stock, plaintiff's personal reliance on misstatements or omissions may be irrelevant in establishing causation).

[192] 391 F. Supp. at 1282.

[193] *Id.*

[194] [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 (S.D.N.Y. Nov. 30, 1979).

failed to rely to their detriment on any alleged misrepresentations.[195] The plaintiffs were thus never in a position to decide whether to tender.[196] Presumably, if there is an actual tender offer, the *Lewis* rationale allows misstatements made during the pre-tender offer period to be actionable under section 14(e).

Support for the *Lewis* decision lies in the fact that Congress enacted section 14(e) for the protection of target shareholders during a tender offer.[197] Without a tender offer the harm section 14(e) seeks to prevent cannot occur. A target shareholder cannot rely on alleged misrepresentations unless the shareholder has the opportunity to decide whether to tender. Without such an opportunity, section 14(e) is inapplicable.

The court decisions of this past year have been less than adequate in defining prohibited tender offer practices. The virtual agreement to extend standing to sue to the non-tendering shareholder is shadowed by the fact that a court may hold that a non-tenderor has not relied on any misrepresentation. Moreover, the scope of the federal securities laws is not defined with any precision so that actionable conduct is not identifiable absent an examination of the philosophy of the relevant court with respect to the proper balance between federal and state control of corporate activity.

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[195] *See* text accompanying notes 124-30 *supra*.

[196] [Current] FED. SEC. L. REP. (CCH) ¶ 97,195 at 96,570. The *Lewis* plaintiffs argued that there would have been a successful tender offer but for the target management's misrepresentations. *Id.* Plaintiffs' argument was thus not a claim of reliance on the part of any target shareholder, but merely a claim that the defendants' conduct disrupted the tender offer. This conduct is not actionable under § 14(e). *See* Rediker v. Geon Indus., Inc., 464 F. Supp. 73, 79 (S.D.N.Y. 1978) (target management's misdeeds may have caused cancellation of tender offer, but claimed injury resulted from cancellation and not from shareholders' reliance on alleged misrepresentations).

[197] *See* text accompanying note 33 *supra*.