Poison Pills: Are Dead Hand Pills Dead In Georgia?

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COMMENT

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I. INTRODUCTION

Market volatility, market volatility, market volatility—there seems to be no end in sight to the monthly, weekly, and daily fluctuations in financial markets around the globe. One interesting implication created by this volatility is a resurgence of takeover fear. When stock prices fall, valuations fall, expectations may be lowered, and healthy, well-valued companies are presented with excellent buying opportunities. As a result, a company that had been growing exponentially may suddenly find itself under the shadow of a tender offer. Therefore, because of recent market volatility, corporate boardrooms have been forced to review and revamp certain defensive mechanisms. This Comment focuses on one defensive strategy and the recent developments regarding its use: the poison pill with continuing director provisions, namely "dead hand" and "no hand" poison pills.

First, this Comment will address the historical aspect of the poison pill as a takeover defense. Primarily, this section will highlight the origin of the poison pill, its mutations, operation and validation, and then more specifically analyze the particular species of poison pills that incorporate continuing director provisions.

Second, this Comment will outline recent developments in the case law regarding continuing director features in poison pills. The United States District Court for the Northern District of Georgia upheld a Georgia corporation's use of a poison pill with a continuing director feature in July 1997.[1] However, in 1998 two separate cases made their way through the Delaware court system and essentially invalidated both the dead hand and no hand mutations of the poison pill.[2]

Third, this Comment will analyze the reasoning that produced the Georgia and Delaware split. While the Georgia opinion was exclusively rooted in the Georgia Business Corporations Code ("GBCC"), the Delaware decisions not only analyzed the plain meaning of Delaware General Corporation Law ("DGCL") but also evaluated the rights plans under the scrutiny of the traditional business judgment rule.

In conclusion, this Comment will highlight possible ramifications of the Delaware decisions on Georgia jurisprudence and provide some insight for advising a corporate board of directors.

II. HISTORICAL PERSPECTIVE ON POISON PILLS

This section will (1) define basic terms associated with poison pills, (2) provide a brief introduction to the various types and features of poison pills, (3) examine a pill's operation and effect, (4) detail the legal validation of the poison pill, and (5) evaluate the impact of continuing director provisions and identify common criticisms.

A. *Terminology*

Terminology is essential to understand the perplexing aspects of a poison pill. As identified in *The Delaware Law of Corporation and Business Organizations*, poison pills are within the category of rights plans.[3] While poison pills appear to have endless variations and antidotes to each of those variations, the basic rights plan, or preferred share purchase rights plan, empowers a board of directors to issue rights for a new series of preferred stock in certain situations usually called

1. Invacare Corp. v. Healthdyne Technologies, Inc., 968 F. Supp. 1578 (N.D. Ga. 1997).

2. Mentor Graphics Corp. v. Quickturn Design Sys., Inc., Nos. 16584, 16588, 1998 WL 839079 (Del. Ch. Dec. 3, 1998) and Carmody v. Toll Bros., Inc., No. 15983, 1998 WL 418896 (Del. Ch. July 24, 1998). Although these cases have virtualy eliminated the legality of the dead hand pill, the issue has not gone away. John Mauser, *Dead-Hand Poison Pill Comes Back to Life in Merger Fight* (visited Mar. 19, 1999) <http://www.lawnewsnetwork.com/stories/mar/e031699c.html>.

3. R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, THE DELAWARE LAW OF CORPORATIONS AND BUSINESS ORGANIZATIONS § 6.47 (3d ed. 1988).

"triggering events."[4] Even though the preferred stock will have both dividend and liquidation preferences, the real impact of these preferred stock rights rests in the exercise or the mere threat of exercise of those rights.[5]

A typical triggering event occurs when a certain percentage (e.g., twenty percent) of the company's common shares is acquired.[6] Once triggered, each poison pill right will attach to one share of common stock, and then

> the rights may be exchanged for the new preferred upon the payment of the [nominal] exercise price. Moreover, if a merger or consolidation occurs under the terms of which the target company's common shares are exchanged for securities of the acquiror, the right "flips-over" and enables the holder, at the then exercise price of the right, to purchase common stock of the acquiror at a price reflecting a market value of twice the exercise price of the right. Thus the right holder would be entitled to purchase $200 worth of the acquirors's common for $100. The resultant dilution of the acquirors's capital is immediate and devastating.[7]

Poison pills that interfere with future directors' powers are commonly known as dead hand and no hand poison pills. The no hand poison pill, or rights plan of limited duration and scope, may also be referred to as a deferred redemption plan with a delayed redemption provision ("DRP").[8] As explained in Sections II and III *infra*, controversy surrounds all three. In essence, the dead hand provision permits no director other than a director who implemented the poison pill to vote on redeeming the rights issued by that poison pill.[9] Similarly, the no hand, or DRP provision, prevents any director, old or new, from redeeming the rights issued pursuant to the poison pill.[10] Both pills effectively counter the immediate and essential ability of corporate raiders to replace an existing hostile board and redeem the outstanding rights.

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4. 19 AM. JUR. 2D *Corporations* § 2605 (1986).
5. *Id.*
6. *Id.*
7. *Id.* (using a "flip-over" poison pill as an example).
8. *Mentor Graphics*, 1998 WL 839079, at *1.
9. *Id.*
10. *Id.*

B. Types of Poison Pills

Basic types of poison pills fall into the categories of flip-in, flip-over, and back-end plans.[11] However, the purpose of this Comment is not to analyze the evolution of poison pills in general, but rather to analyze one particular variation of the poison pill—those with continuing director provisions. More elaborate and detailed articles about the evolution of poison pills and their numerous features are readily available.[12]

C. Operation of the Pill

The operation of a poison pill may be summarized by the election, the effect, and the redemption. The election is straightforward. A board of directors uses the poison pill as one of its available defensive measures by voting for a preferred share rights plan during a scheduled meeting of the board. After an affirmative vote, the poison pill is created and generally recorded as a board resolution or in the company bylaws. Once established, the poison pill's effect is immediate.

Until the poison pill is redeemed, any potential acquiring company or corporate raider must avoid triggering the poison pill because its effect is to dilute their newly acquired stock.[13] As described in Section II.A *supra*, the exercise of poison pill rights effectively cuts stock value in half. Therefore, corporate raiders are forced to devise schemes to avoid the poison pill's negative effect. As expected, they have accomplished this feat in several ways.

A fundamental method used to avoid dilution is redemption. Once the pill is redeemed, the rights can no longer affect the stock because they are no longer exercisable. Currently, a poison pill or rights plan may be redeemed only by the board of directors.[14] A board may redeem issued rights in several ways. First and foremost, the acquisition may be nonhostile, in which case the board of directors would simply redeem the

11. Laura L. Cox, Comment, *Poison Pills: Recent Developments in Delaware Law*, 58 U. CIN. L. REV. 611, 615-18 (1989).

12. *Id.*; *see also* J. Kurt Denkewalter, Comment, *Poison Pills: Is the Flip-In Flipping Out?*, 14 U. DAYTON L. REV. 701 (1989); Jeffrey N. Gordon, *"Just Say Never?" Poison Pills, Deadhand Pills, and Shareholder-Adopted Bylaws: An Essay for Warren Buffett*, 19 CARDOZO L. REV. 511 (1997).

13. *See supra* note 4-7.

14. It should be duly noted that a current debate exists regarding whether shareholders may force directors to redeem poison pills or rights plans. For excellent commentary on this issue, see Lawrence A. Hamermesh, *Corporate Democracy and Stockholder Adopted By-Laws: Taking Back the Street?*, 73 TUL. L. REV. 409 (1998); John C. Coffee, Jr., *The Bylaw Battlefield: Can Institutions Change the Outcome of Corporate Control Contests?*, 51 U. MIAMI L. REV. 605 (1997).

rights as part of a friendly deal.[15] Second, the acquiring company may purchase amounts of stock up to a tenth of a percentage below the triggering point and then wage a proxy contest to replace the target board and have the new board redeem the rights.[16] Either way, a pill must be redeemed before acquisition, or the operation could nullify the anticipated gains or synergies created.

D. Legality of the Poison Pill

Beginning in the early 1980s, poison pills started to be considered as an effective defensive takeover mechanism, and in 1985, the poison pill "ma[de] its legal debut"[17] in both *Unocal Corp. v. Mesa Petroleum Co.*[18] and *Moran v. Household International, Inc.*[19]

In *Unocal* the Supreme Court of Delaware squarely answered whether boards of directors opposing current takeover threats may be protected by the business judgment rule.[20] After Mesa Petroleum proposed a two-tier tender offer for sixty-four million shares of Unocal's outstanding stock, Unocal's board of directors held two board meetings to analyze the offer. After concluding that Mesa's offer was inadequate, Unocal's board approved an exchange offer that would effectively stop Mesa from acquiring Unocal and provide shareholders with an alternative worth approximately forty percent more than the Mesa offer.[21] The issues raised in this case were whether Unocal's board was presented with a "threat it reasonably perceived to be harmful to the corporate enterprise, and if so, [whether] its action [was] entitled to the protection of the business judgment rule."[22]

The Delaware Supreme Court answered both questions in the affirmative.[23] The court concluded the following: (1) that "in the broad context of corporate governance, including issues of fundamental corporate change, a board of directors is not a passive instrumentality;"[24] (2) that there is a heightened duty when "a board may be acting

15. Shawn C. Lese, Note, *Preventing Control from the Grave: A Proposal for Judicial Treatment of Dead Hand Provisions in Poison Pills,* 96 COLUM. L. REV. 2175, 2181-82 (1996).

16. For a full discussion, see *supra* notes 11-12.

17. *Mentor Graphics*, 1998 WL 839079 at *1.

18. 493 A.2d 946 (Del. 1985).

19. 500 A.2d 1346 (Del. 1985).

20. 493 A.2d at 953.

21. *Id.* at 949-51.

22. *Id.* at 953.

23. *Id.* at 958.

24. *Id.* at 954 (citations omitted).

primarily in its own interests, rather than those of the corporation;"[25] and (3) that corporate directors have both a fiduciary duty and a duty of care.[26] In sum, the court held that in order for a board of directors to receive the benefit of the business judgment rule for their actions regarding defensive mechanisms, the board must (1) act in "good faith," (2) conduct a "reasonable investigation pursuant to a clear duty to protect the corporate enterprise," and (3) create a defensive mechanism that "is reasonable in relation to the threat that the board rationally and reasonably believed" was being posed.[27]

In *Household*, decided just five months after *Unocal*, the Supreme Court of Delaware validated Household International Inc.'s rights plan by holding that adopting the plan was "a legitimate exercise of business judgment" by the board of directors.[28] In the decision's concluding paragraphs, the court's analysis mirrored that of *Unocal*.[29] Although Household's plan was upheld, the court did not answer whether the directors had *used* the plan in a permissible fashion because the plan had yet to be used.[30]

Household's board of directors adopted a preferred share purchase rights plan ("Rights Plan").[31] This Rights Plan was "a defensive mechanism adopted to ward off possible future advances and not a mechanism adopted in reaction to a specific threat."[32] As such, the court identified the primary issues to be (1) whether the directors were within their power and authorization to adopt the rights plan and (2) whether the directors would be protected under the business judgment rule.[33]

The Delaware Supreme Court answered both issues in the affirmative.[34] First, the court concluded "that sufficient authority for the Rights Plan exist[ed] in 8 *Del.C.* § 157."[35] Therefore, "the inherent powers of the Board conferred by 8 *Del.C.* § 141(a), concerning the management of the corporation's 'business and *affairs*' also provid[ed] the Board additional authority upon which to enact the Rights Plan."[36]

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25. *Id.*
26. *Id.* at 955.
27. *Id.* at 958.
28. 500 A.2d at 1348.
29. *Id.* at 1357.
30. *Id.*
31. *Id.* at 1348.
32. *Id.* at 1350.
33. *Id.*
34. *Id.* at 1357.
35. *Id.* at 1353.
36. *Id.*

Second, the court concluded that because the directors were well informed and their decision was well reasoned, "the Household Directors receive the benefit of the business judgment rule in their adoption of the Rights Plan."[37]

In *Unitrin, Inc. v. American General Corp.*,[38] the Delaware Supreme Court clarified whether and how a board of directors' response to a takeover threat was within the tests set forth in *Unocal* and *Household*.[39] In *Unitrin* American General publicly announced a merger with Unitrin, and, in response, Unitrin's board of directors implemented a repurchase program as a defensive mechanism.[40] Unitrin's board did so for four stated reasons: (1) Unitrin's stock was more valuable than American General's offer; (2) American General's offer failed to recognize long term benefits of Unitrin as an independent company; (3) Unitrin's strong financial position, and not current stock price, was the true value; and (4) the merger would likely violate antitrust laws and statutes.[41] Although the reasoning should have been identical to the reasoning in *Unocal*, the Court of Chancery erroneously created a judicial standard that analyzed whether the particular defensive strategy employed by Unitrin was "a necessity."[42] However, the Supreme Court of Delaware clarified and reaffirmed the enhanced scrutiny required under the *Unocal* standard.[43] The necessity of the defensive strategy should never have been at issue; but rather, "the *Unocal* standard of enhanced judicial scrutiny [should have been] applied to the defensive actions of the Unitrin defendants in establishing the poison pill and implementing the Repurchase Program."[44] Therefore, the court reversed and remanded the case to apply *Unocal's* three-prong test.[45]

After these three cases were decided, the judicial standard for scrutinizing particular board-implemented defensive measures was firmly imbedded in corporate law. Naturally, boards of directors were creative and formulated different techniques to hinder, if not altogether freeze, potential corporate raiders from taking over their corporations. Several creative solutions that incorporate the protection of continuing director provisions have recently been litigated.

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37. Id at 1357.
38. 651 A.2d 1361 (Del. 1995).
39. *Id.* at 1367.
40. *Id.* at 1366-67.
41. *Id.* at 1370.
42. *Id.* at 1391.
43. *Id.*
44. *Id.*
45. *Id.*

E. Impact of the Continuing Director Provisions

As already identified, two examples of poison pills with continuing director provisions are dead hand pills and no hand, or DRP, pills. Essentially, these pills trap the power to redeem the pill's rights in the board members who adopt the plan and/or establish a particular time period during which no new board or board members may redeem rights.[46] The effect is obvious. With the dead hand provision, an acquiring company could take control of a target board, but the newly formed board would not be able to redeem the exercise or repurchase rights. Similarly, if there is a period of delay due to a no hand provision, any redemption may be so distant that the new board would not want to risk the possibility of shareholders exercising their rights during the interim. In the face of such restrictions and risks, the takeover may be ineffective because of the dilution powers of the pill, and may never become a reality.

One of the first cases to examine continuing director provisions was *Bank of New York Co. v. Irving Bank Corp.*[47] In 1988, Irving Bank Corporation's rights agreement restricted actions of future boards of directors regarding the redemption of the issued rights.[48] The New York state court flatly invalidated the provision based upon the underlying discriminatory effect on the powers that present and future boards would possess.[49] However, the court ruled purely on a statutory basis and expressly did not discuss issues regarding the directors' fiduciary duties or the business judgment rule.[50] Thus, there was a marked period during which speculation about the Delaware court's disposition of continuing directorships under general corporate principles ruled corporate jurisprudence.[51] Most of the speculation and commentaries concluded that continuing directorship provisions should be prohibited not simply on statutory grounds, but primarily based on policy concerns and shareholder rights theories.[52]

46. *See* Nos. 16584, 16588, 1998 WL 839079 (Del. Ch. Dec. 8, 1998).
47. 528 N.Y.S.2d 482 (N.Y. Sup. Ct. 1988).
48. *Id.* at 483.
49. *Id.* at 486.
50. *Id.*
51. *See* Lese, *supra* note 15.
52. *Id.*; Recent Case, 111 HARV. L. REV. 1626 (1998).

III. RECENT DEVELOPMENTS

This section will first address the Georgia case that upheld the use of a continuing director provision[53] and then address the opposite stance adopted by the Court of Chancery of Delaware.[54] In the summer of 1997, the debate over continuing director provisions was rekindled. This time, the United States District Court for the Northern District of Georgia analyzed a shareholders rights plan that had a continuing director feature.[55] The court held that under the GBCC, Healthdyne's board of directors did not breach its fiduciary duties and exercised proper discretion in implementing a continuing director feature in its poison pill.[56] As such, the court granted the company's motion for summary judgment.[57]

In *Invacare Corp. v. Healthdyne Technologies, Inc.*, Healthdyne, a Georgia corporation, received an all-cash tender offer that the board of directors believed to be "grossly inadequate."[58] At the time of the tender offer, Healthdyne had a shareholders rights plan that included a continuing director feature.[59] In essence, this feature "require[d] that any redemption or amendment of the rights plan be approved by one or more directors who were members of the Board prior to the adoption of the rights plan, or who were subsequently elected to the Board with the recommendation and approval of the other continuing directors."[60] Therefore, "if Healthdyne's shareholders [were to vote] to replace the incumbent directors with Invacare's slate of directors, the new Board of Directors could not redeem the rights plan because they would not be 'continuing directors.'"[61]

Invacare sought a preliminary injunction to invalidate the continuing director feature. Invacare also proposed a bylaw to be adopted at Healthdyne's annual meeting that would force Healthdyne's board to repeal the continuing director feature.[62] Not only did the court deny Invacare's preliminary injunction, but it granted summary judgment in

53. Invacare Corp. v. Healthdyne Tech., Inc., 968 F. Supp. 1578 (N.D. Ga. 1997).
54. Mentor Graphics Corp. v. Quickturn Design Sys., Inc., Nos. 16584, 16588, 1998 WL 839079, at *1 (Del. Ch. Dec. 3, 1998).
55. 968 F. Supp. at 1579.
56. *Id.* at 1581.
57. *Id.* at 1582.
58. *Id.* at 1579.
59. *Id.*
60. *Id.*
61. *Id.*
62. *Id.*

favor of Healthdyne, declaring Invacare's proposed bylaw in violation of Georgia corporate laws.[63]

In its reasoning, the district court "note[d] that Georgia corporate law embraces the concept of continuing directors as part of a defense against hostile takeovers."[64] More specifically, Georgia "statutes recognize a benefit to shareholders in not allowing a hostile bidder to acquire a corporation by installing its own board of directors to eliminate any takeover defense mechanisms of a rights plan."[65] Focusing on Invacare's proposed bylaw, the court held such a bylaw "would infringe upon the board's discretion [under O.C.G.A. § 14-2-624(c)] by requiring the incumbent Healthdyne board to remove the continuing director provision."[66] Moreover, the court found the proposed bylaw to be "inimical to the corporate structure contemplated by the Georgia Business Corporation Code, which separates the rights and duties of directors from those of the shareholders."[67] In summary, the court held (1) that "the concept of continuing directors is an integral part of a takeover defense and is not contrary to public policy in Georgia"[68] and (2) that "Invacare's proposed bylaw [was] invalid as a matter of law."[69]

While this decision has been expressly[70] and implicitly criticized,[71] it was not, until recently, directly adverse to Delaware law. In August and December of 1998, the Court of Chancery of Delaware took a position contrary to the Georgia decision. In *Carmody v. Toll Brothers*[72] and *Mentor Graphics Corp. v. Quickturn Design Systems, Inc.*,[73] Vice Chancellor Jacobs all but invalidated dead hand and no hand poison pills under Delaware corporate law. Vice Chancellor Jacobs not only attacked the poison pills under a statutory analysis, but more importantly, analyzed the poison pills under the traditional *Unocal, Household,* and *Unitrin* doctrines and held the deferred redemption plan, or no hand poison pill, could not survive judicial scrutiny.[74]

In *Toll Brothers* the Delaware Court of Chancery directly assessed the legality of the dead hand poison pill.[75] At issue was Toll Brothers

63. *Id.* at 1582-83.
64. *Id.* at 1580.
65. *Id.* at 1581.
66. *Id.* at 1582.
67. *Id.*
68. *Id.* at 1581.
69. *Id.* at 1582.
70. Recent Case, *supra* note 52.
71. *See* Lese, *supra* note 16.
72. No. 15983, 1998 WL 418896 (Del. Ch. July 24, 1998).
73. Nos. 16584, 16588, 1998 WL 839079 (Del. Ch. Dec. 8, 1998).
74. *Id.* at *23; 1998 WL 418896, at 13.
75. 1998 WL 418896, at *1.

rights plan.[76] Toll Brothers was founded in 1967, went public in 1986, and adopted a rights plan on June 12, 1997 after contemplating that it might be perceived as a takeover target.[77] The company's board of directors announced it had instituted the rights plan with the dead hand feature "to protect its stockholders from 'coercive or unfair tactics to gain control of the company' by placing the stockholders in a position of having to accept or reject an unsolicited offer without adequate time."[78] The rights plan distributed a dividend of "one preferred stock purchase right (a 'Right') for each outstanding share of common stock" and would upon a triggering event "entitle [the Right holder] to buy two shares of Toll Brothers common stock or other securities at half price."[79] Thus, the Rights created the dilution power typical of most poison pills.

The novelty of Toll Brothers' rights plan was in its dead hand feature. "In substance, the 'dead hand' provision operate[d] to prevent any directors of Toll Brothers, except those who were in office as of the date of the Rights Plan's adoption (June 12, 1997), or their designated successors, from redeeming the Rights until they expire[d] on June 12, 2007."[80] Carmody's complaint alleged the dead hand feature not only removed a proxy contest from a corporate raider's quiver, but disenfranchised shareholders because they could not vote for any directors other than incumbents.[81] Thus, the court narrowed the issue to "whether a 'dead hand' provision in a 'poison pill' rights plan is subject to legal challenge on the basis that it is invalid as ultra vires, or as a breach of fiduciary duty, or both."[82] After reviewing the historical and legal aspects of poison pills, the court turned to the validity of the dead hand provision.

Toll Brothers' continuing director provision classified directors as either having a power to redeem the pill or not to redeem the pill.[83] The court held that this difference in redemption power created separate classes of directors.[84] Under the DCGL, when multiple classes of directors are intended, this distinction must be listed in the company's certificate of incorporation.[85] However, because no such distinction was

76. *Id.*
77. *Id.*
78. *Id.*
79. *Id.* at *2. In this case, the "event [was] the acquisition of 15% or more of Toll Brothers' stock by any person or group of affiliated or associated persons." *Id.*
80. *Id.* at *3.
81. *Id.*
82. *Id.*
83. *Id.* at *9.
84. *Id.*
85. *Id.*

listed in Toll Brothers' certificate of incorporation, "the 'dead hand' feature of the Rights Plan [was] ultra vires, and hence, statutorily invalid under Delaware law."[86] Moreover, the dead hand provision "would interfere with the board's power to protect fully the corporation's (and its shareholders') interests in a transaction that is one of the most fundamental and important in the life of a business enterprise," namely, the ability to achieve the business combination desired.[87] Finally, the Court of Chancery held "the 'dead hand' feature violated [Toll Brothers' board of directors'] fiduciary duty of loyalty" because (1) it "purposefully interfere[d] with the shareholder voting franchise without any compelling justification,"[88] and (2) the defensive measure of the dead hand provision was "'disproportionate' . . . because it either preclude[d] or materially abridge[d] the shareholders' rights to receive tender offers and wage a proxy contest to replace the board."[89] Although the court struck Toll Brothers' continuing director provision on a purely statutory basis, the court further supported its conclusion under a fiduciary duty analysis.[90]

In December 1998 the Delaware Court of Chancery further tightened the screws to boards of directors relating to their fiduciary duties in implementing defensive mechanisms. *Mentor Graphics Corp. v. Quickturn Design Systems, Inc.*, focused on Quickturn's board's implementation of the poison pill's "most recent incarnation—a 'no-hand' poison pill of limited duration and scope."[91] In essence, the no hand poison pill "would evenhandedly prevent all members of a newly elected target board, whose majority is nominated or supported by the hostile bidder, from redeeming the rights to facilitate an acquisition by the bidder . . . for six months after the new directors take office."[92] The court also assessed the validity of a bylaw amendment instituted by Quickturn's board, in which the board delayed "the holding of any special stockholders meeting requested by stockholders for 90 to 100 days after the validity of the request [was] determined."[93]

Quickturn's board had eight members who collectively owned approximately five percent of Quickturn's common stock, and all but one

86. *Id.*
87. *Id.* at *10.
88. *Id.* This prong of a fiduciary duty test was created in *Blasius Ind., Inc. v. Atlas Corp.*, 564 A.2d 651 (Del. Ch. 1988). *Blasius* dealt with general director fiduciary duties and specifically did not relate to a poison pill. *Id.*
89. 1998 WL 418896, at *11.
90. *Id.*
91. 1998 WL 839079, at *1.
92. *Id.*
93. *Id.*

were outside directors. On August 12, 1998, Mentor Graphics announced a cash tender offer for all of Quickturn's outstanding stock at roughly a fifty percent premium. The next day, Quickturn's board of directors met to evaluate the offer and devise a strategy for further analysis and action. The board met on three separate days to thoroughly analyze the offer. On August 21, 1998, the board rejected Mentor's offer because it felt that the tender offer was undervalued and inadequately priced.[94]

In addition to rejecting the tender offer, Quickturn's board instituted the following defensive measures: (1) it amended the bylaws to extend the notice required for a special stockholder meeting, and (2) it amended the rights plan by substituting the DRP in lieu of the existing dead hand provision.[95] Coupled together, the defense tactics effectively extended any possible redemption of the pill to nine months—three months for the bylaw amendment and six months for the expiration of the DRP.[96]

Addressing the bylaw amendment first, the court narrowed the issue to the following: "whether the Amendment, standing alone, falls outside any range of potentially reasonable responses to that threat [whereby a hostile bidder could call a special meeting to railroad stockholders] and therefore constitutes a disproportionate response to the threat posed by the Mentor Offer and proxy contest."[97] Vice Chancellor Jacobs upheld the bylaw amendment on two grounds.[98] First, advance notice was reasonable and in line with the time requirement for special meetings in other sections of company bylaws.[99] Second, mandatory time periods for advance notice are "commonplace" in Delaware jurisprudence.[100]

As for the DRP, Mentor attacked Quickturn's amendment to the rights plan on three grounds.[101] First, Mentor alleged that Quickturn violated fiduciary duties by "interfering with the Quickturn shareholders' right to elect a board of their choice."[102] Second, Mentor contended that "the DRP was a disproportionate response to any threat reasonably perceived" and thus violated *Unocal* and *Unitrin*.[103] Third, Mentor argued that under plain statutory interpretation, the DRP would be

94. *Id.* at *2-7.

95. *Id.* at *7. The assumption is that the legal advisors to Quickturn's board were well aware of the decision in *Toll Brothers* decided that same month.

96. *Id.*

97. *Id.* at *12.

98. *Id.* at *13.

99. *Id.* at *14.

100. *Id.*

101. *Id.* at *15.

102. *Id.*

103. *Id.*

invalid, like the dead hand provision in *Toll Brothers*.[104] The court ruled on Mentor's second contention[105] and held that Quickturn's DRP failed the *Unocal* and *Unitrin* standards of enhanced scrutiny relating to the perceived threat and proportionality of the response.[106] Essentially, the court held the effect of the DRP could not "be reconciled with the directors' stated justification for adopting it."[107] The court provided the following hypothetical to support its conclusion:

> Suppose that the day after the new Mentor-nominated board takes office, a third party makes a $14 per share offer, which tops Mentor's $12.125 bid. An auction then ensues. Mentor decides to increase its offer to $15, and becomes the high bidder. Under the DRP, the new board could redeem the pill and accept the $14 bid immediately, but could not accept Mentor's $15 bid for six months.[108]

Therefore, the court held that the perceived threat and the solution to avoid that threat were inconsistent.[109] Second, the DRP failed "the proportionality test because its articulated purpose—to give a newly elected board time to inform itself of Quickturn's value—would already have been achieved by the conclusion of the three month delay period imposed by the By-Law Amendment."[110] Thus, the DRP defense implemented by Quickturn's board was declared invalid.[111] In sum, the court upheld the directors' bylaw amendment but rejected their rights plan amendment.[112]

As evidenced by the holdings in *Toll Brothers* and *Mentor Graphics* a definite split now exists between Georgia and Delaware courts. While Georgia has upheld continuing director provisions, Delaware seems to have clearly rejected their validity. Many states may soon be forced to analyze similar issues under their state corporation codes. At the center of the debate, however, still looms the age-old conflict of director power versus shareholder power and the disagreement over exactly which directors (old or new) should possess the right to redeem shares.

104. *Id.*

105. After the DRP was invalidated under the second contention, the court found it unnecessary to analyze either the first or third claim. *Id.* at *16.

106. *Id.*

107. *Id.* at *22.

108. *Id.*

109. *Id.*

110. *Id.*

111. *Id.* at *23.

112. *Id.*

IV. CONCLUSION

Pursuant to the cases in this Comment, a corporate board of directors has greater latitude available under Georgia law than under Delaware law. The decision in *Toll Brothers* most clearly articulated this discrepancy. Whereas Delaware and New York corporate statutes require "limitations upon the directors' power be expressed in the corporation's charter,"[113] the Georgia corporate code does not.[114] Thus, the Delaware Court of Chancery would not recognize Toll Brothers' reliance on *Invacare* because "[t]he relevant Delaware corporate statutory scheme, like New York's, differs materially from that of Georgia."[115] However, in light of *Mentor Graphics* and *Toll Brothers*, it is important to highlight language in the comment to the Georgia statute that gives a Georgia board of directors sole discretion over the issuance of rights, options, or warrants.[116] In the comment, the drafters state that "[t]he language was intended to permit the approach of courts interpreting Delaware law, including the Delaware Supreme Court in *Moran v. Household International, Inc.*, . . . which have held that the board of directors is authorized to issue rights pursuant to shareholder rights plans."[117] Following the intent of the drafters to stay in line with Delaware decisions, the statutory differences between Georgia and Delaware may no longer protect a Georgia board of directors as it did before the decisions in *Mentor Graphics* and *Toll Brothers*.

Regardless, Georgia has been, and seemingly will remain, proincumbent board when continuing director provisions are at issue. Individual investors and fund groups continue to attempt to exercise influence over corporate matters that have traditionally been decided in the board room. While involvement by investors may be beneficial in many respects, expect more challenges to defensive mechanisms—especially those that reserve special powers for current board members.

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113. 1998 WL 418896, at *10.
114. *Id.* at *11 n.41.
115. *Id.*
116. O.C.G.A. § 14-2-624(c) cmt. (1994).
117. *Id.*