

“We had reached a whole new plateau of hostile takeovers, and there was really very little in the way of defense to them.”

– Martin Lipton in 2010 on why he created the poison pill

Street Wise

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History of the Poison Pill

The shareholder rights plan (“poison pill”) has been called “the most important innovation in corporate law since Samuel Calvin Tate Dodd invented the trust for John D. Rockefeller and Standard Oil in 1879”.

In 1982, in response to two hostile takeover battles in Texas, Martin Lipton, one of the godfathers of the modern M&A advisory business and founding partner of Wall Street’s most illustrious law firm, Wachtell, Lipton, Rosen & Katz, developed the idea for the poison pill defense.

Lipton’s goal was to improve corporate governance and “level the playing field” by providing boards a line of defense against activist investors. His theory was influenced by the seminal intellectual of corporate law, Adolf Berle, under whom he studied after law school.

In 1985, the Delaware Supreme Court ruled in *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.* that the adoption of the pill was a proper exercise of board authority. Over the coming years, the poison pill became the primary line of defense for corporate boards as corporate raiders, leverage buyout artists and junk bond financiers transformed Wall Street from a place of relationship bankers to activist investors.

In 2010, this precedent was challenged in *Air Products & Chemicals, Inc. v. Airgas, Inc.* The Delaware Court of Chancery, the country’s most influential court overseeing business cases, upheld the 25 year precedent and ruled that the Airgas board acted in good faith and with reasonable facts. Since this ruling, the poison pill continues to evolve.

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Poison Pill Primer

Carl Icahn v. Netflix

On Monday, November 5, Netflix adopted a shareholder rights plan (“poison pill”) as a protection against activist shareholder Carl Icahn, who acquired a 9.98 percent stake in the company. While adoption of poison pills against activist shareholders—and Carl Icahn in particular—is nothing new, Netflix’s approach to the poison pill is.

The company created two tiers at which the pill would be activated: one for passive shareholders, which is 20 percent, and one for activist shareholders, which is 10 percent—5 percent lower than a typical threshold. By creating two tiers, the company has created a structure that protects the board against activist investors acquiring a large stake while allowing mutual funds and other investors the opportunity to still acquire large stakes in the company for their portfolios.

This approach, Netflix argues, is shareholder-friendly. Icahn, however, disagrees, claiming that the decision should be brought to the shareholders for a vote, which is the law in most of Europe but not in the United States.

Poison Pill Definition

A shareholder rights plan, also known as a poison pill, is an action taken by the board of directors to help prevent a takeover from an outside bidder. It entails issuing a right to existing shareholders, excluding the bidder, to purchase additional shares of common or preferred shares. The plan goes into effect when a bidder acquires a predetermined number of shares.

Tobin & Company Services

Tobin & Company advises and prepares clients for potential unsolicited acquisition attempts. In helping boards develop a takeover defense strategy, the firm advises clients on the potential impact that the creation or extension of a plan has on shareholder value and provides recommendations regarding the exercise price for the plan. Tobin & Company also conducts a market analysis of the client’s susceptibility to a takeover attempt.