THE RISE OF CORPORATE TAKEOVERS IN THE PHILIPPINES: LEARNING OUR LESSONS FROM THE UNITED STATES AND JAPAN*

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ABSTRACT

Hostile takeovers are rarely seen in the Philippines. However, the fact that hostile takeovers are already happening in the Philippines should be a cause for concern in the corporate world. With hostile takeovers comes the inevitability of litigations concerning the legality of anti-takeover measures undertaken by management.

At present, Philippine courts have had no occasion to rule on the legality of said measures. The only standard of review existing in Philippine corporate law jurisprudence on anti-takeover measures is the business judgment rule. As will be shown in this paper, the said rule is not a sufficient standard.

The purpose of this paper is to examine the standards of review being used in the world's two largest economies: the United States and Japan. The author will then endeavor to make some recommendations on how to deal with anti-takeover measures in the Philippine context using the valuable lessons learned from the world's two largest economies.

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I. INTRODUCTION

The raiders are here! Just recently, the Philippines saw the bitter battle for the takeover of Equitable PCI Bank, the country's third largest bank, by Banco De Oro, the country's seventh largest. To be sure, the number of hostile takeovers in the Philippines to date is small compared to advanced economies.[1] The mere existence of hostile takeovers, however, should be a cause for concern in the Philippine corporate setting, taking into account the potential changes they may bring about.

One of the problems that have to be addressed in a hostile takeover scenario is the potential abuse by management in adopting defense mechanisms to thwart a hostile takeover. But how are we to determine whether or not there has been an abuse by management in adopting defensive measures?

This paper will endeavor to answer this question. The author will examine the standards of review which have been applied to hostile takeover defenses in the two largest economies, namely, the United States and Japan, with the aim of determining the proper standard which should be used in the Philippines taking into account the peculiarity of the Philippine corporate system.

Part II will give an overview of takeovers in the Philippines, including definitions of terminologies, methods of effecting takeovers and kinds of takeovers. Part III will discuss how takeovers are dealt with in the Philippines. Discussions on take over bid regulations and anti-takeover measures are included in this portion. Part IV will make a very brief summary of standards of review of anti-takeover measures in the United States and Japan. Part V will make a forecast as to how Philippine courts will review anti-takeover measures. Part VI will contain, among others, the author's recommendation on the proper standard of review to be used in the Philippines taking into account valuable lessons from the United States and Japan. Part VII contains the author's conclusion.

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[1] Hostile takeovers are not common in the Philippines because most company shares are not publicly listed and controlling interest tends to remain with a small group of parties. Cross-ownership and interlocking directorates among listed companies also lessen the likelihood of hostile takeovers.

In fact, the number of hostile takeover deals in the Philippines is too small that the Philippine Securities and Exchange Commission (SEC) does not have statistics on said deals.

II. BACKGROUND

A. THE PHILIPPINES AND M&A[2]

The Philippines does not have specific M&A legislation. Generally, the provisions of the Corporation Code and the Civil Code will govern M&A transactions. In the case of international M&A transactions, the Foreign Investments Act[3] will govern the entry of foreign investments in the Philippines.

B. KINDS OF TAKEOVERS

1. Friendly Takeovers

A corporate takeover can be friendly or hostile. A friendly takeover is one where the target firm's management and board of directors are in favor of the takeover. In a friendly takeover, target management supports the takeover. A friendly overture suggesting some kind of benefit from combining the two companies may be made. For example, synergistic gains that may result from combining one corporation's particularly good product line with the marketing and distribution strengths of another corporation may be mentioned. After discussions and negotiations, an arrangement between the two companies may be worked out.

There are different ways to achieve friendly corporate takeovers in the Philippines. These include (i) merger, (ii) consolidation, (iii) sale of substantially all corporate assets and purchase thereof by another

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[2] In this paper, the terms M&A and takeover are used interchangeably.

[3] Rep. Act No. 7042. This is An Act to Promote Foreign Investments, Prescribe the Procedures for Registering Enterprises Doing Business in the Philippines and for other Purposes, as amended.

The Foreign Investments Act generally governs foreign investments in the Philippines. There are also several pieces of special investment legislation that complement the Foreign Investments Act and demonstrate government efforts to create an investment climate conducive to foreign investment. (This portion was taken from Quisimbing Toress Philippines Guides to Mergers and Acquisitions 2004/2005, page 1. A copy of this guide can be downloaded at http://www.bakernet.com/NR/rdonlyres/A8547C2-ED1B-4105-9400-CDB4F2AD0ABF/35295/Philippines200405.pdf.

The Board of Investments, an agency attached to the Department of Trade and Industry, is the lead agency of the Philippine government in investment promotions. The Board of Investment has a comprehensive promotion program that aims to minimize investment barriers and facilitate the establishment of business ventures throughout the country. The Board of Investments is mandated to draw up an Investment Priorities Plan that, among other things, includes a list of investment areas or activities that are eligible for fiscal and non-fiscal incentives.

corporation, and (iv) equity acquisition or the acquisition of all or substantially all of the stock of one corporation from its stockholders in exchange for the stock of the acquiring corporation.[4] Another type of transaction is the (v) acquisition of a business enterprise.[5]

Asset Acquisition

In an asset acquisition, the purchaser is only interested in the "raw" assets and properties of the business.[6]

Business Enterprise Acquisition

In a business enterprise acquisition, the purchaser's interest is essentially to obtain the "earning capability" of the venture.[7]

Equity Acquisition

In an equity acquisition, the purchaser takes control and ownership of the business by purchasing the shareholdings of the corporate owner.[8]

Mergers and Consolidations

Express authority to merge or consolidate has been granted to all corporations under Section 76 of the Corporation Code.[9] On the other hand, mergers or consolidations involving foreign

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[4] Jose Campos Jr. & Maria Clara L. Campos, THE CORPORATION CODE COMMENTS, NOTES, AND SELECTED CASES, VOL. 2 at 440.

[5] A business enterprise comprises more than just the properties of the business, but includes a "concern" that covers the employees, the goodwill, list of clientele and suppliers, etc., which gives it value separate and distinct from its owners or the juridical entity under which it operates. (Cesar Villanueva, PHILIPPINE CORPORATE LAW 597-598 (2001)).

[6] *Id.* at 593. In such an acquisition, the purchaser is not interested in the entity of the corporate owner of the assets, nor of the goodwill and other factors relating to the business itself.

[7] *Id.* at 594. The purchaser in such is not interested in obtaining the juridical entity that owns the business enterprise, and therefore purchases directly the business from the corporate entity. (*Id.*).

[8] *Id.*

[9] § 76 of the Corporation Code provides that "two or more corporations may merge into a single corporation which shall be one of the constituent corporations or may consolidate into a new single corporation which shall be the consolidated corporation."

corporations licensed to do business in the Philippines are expressly authorized under Section 132 of the Corporation Code.[10]

Merger means the absorption of one or more corporations by another existing corporation, which retains its identity and takes over the rights, privileges, franchises and properties of the absorbed corporation(s). The absorbing corporation continues its existence while the life or lives of the other corporation(s) is/are terminated.[11]

By consolidation, what is meant is the union of two or more corporations to form a new corporation, having the combined rights, privileges, franchises and properties of the constituent companies, all combining to lose their corporate existence.[12] Briefly, it is described as the union of two or more corporations into a single new corporation; all the constituent corporations thereby ceasing to exist as separate entities.[13]

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[10] Sec. 132. *Merger or consolidation involving a foreign corporation licensed in the Philippines.* – One or more foreign corporations authorized to transact business in the Philippines may merge or consolidate with any domestic corporation or corporations if such is permitted under Philippine laws and by the law of its incorporation: Provided, That the requirements on merger and consolidation as provided in this Code are followed.

Whenever a foreign corporation authorized to transact business in the Philippines shall be a party to a merger or consolidation in its home country or state as permitted by the law of its incorporation, such foreign corporation shall, within sixty (60) days after such merger or consolidation becomes effective, file with the Securities and Exchange Commission, and in proper cases with the appropriate government agency, a copy of the articles of merger or consolidation duly authenticated by the proper official or officials of the country or state under the laws of which merger or consolidation was effected: Provided, however, That if the absorbed corporation is the foreign corporation doing business in the Philippines, the latter shall at the same time file a petition for withdrawal of its license in accordance with this Title. (Corporation Code).

[11] Rosario Lopez, THE CORPORATION CODE OF THE PHILIPPINES ANNOTATED, VOL. 2 (1994) at 2, *citing* Luis Liwanag II, SEC Opinion, Jun. 11, 1986.

A *de facto* merger is also recognized under Philippine law. A *de facto* merger under the Corporation Code can occur when one corporation acquires all or substantially all of the properties of another corporation in exchange for the shares of stock of the acquiring corporation. The acquiring corporation would end up with the business enterprise of target corporation; whereas the target corporation would end up with basically its only remaining assets being the shares of stock of the acquiring corporation. (Villanueva, *supra* note 5 at 616).

The separate juridical personalities of the constituent corporations would remain, and consequently, the successorship of liabilities under business-enterprise transfers would apply, such that the acquiring corporation would then be liable for the liabilities pertaining to the business enterprise it has acquired.

[12] Lopez, *supra* note 11, at 932.

[13] *Id., citing* Liwanag *supra* note 11.

Similar to consolidation of corporations under American laws, is amalgamation, a word of English origin. Amalgamation takes place when existing corporations agree to abandon their respective articles of association and regulation, and to register themselves under new articles as one body. This would be a

The parties to a merger or consolidation are called *constituent corporations.*[14] In consolidation, all the constituents are dissolved and absorbed by the new consolidated enterprise.[15] In merger, all constituents, except the surviving corporation, are dissolved.[16] In both cases, however, there is no liquidation of the assets of the dissolved corporations, and the surviving or consolidated corporation acquires all their properties, rights and franchises and their stockholders usually become its stockholders.[17]

Merger or consolidation may be horizontal, vertical or conglomerate. It is called *horizontal* when the merger is between competing firms.[18] It is said to be *vertical* if a corporation acquired another corporation which uses or distributes the products of the former.[19] When the merger involves corporations which are neither competing nor otherwise related in the chain of production or distribution, it is called a *conglomerate merger.*[20]

2. Hostile Takeovers

On the other hand, hostile takeovers refer to the taking control of a corporation against the will of its management and/or directors.[21] A bidder prefers a friendly deal because hostile takeovers usually involve greater expense. The bidding process may result in a higher premium because it may involve other bidders bidding the price up.[22] It will also include additional costs such as consulting and legal fees.

One of the ways to effect a hostile takeover is through making a tender offer or takeover bid. Tender offers are bids made directly to stockholders, bypassing management and the board of directors.[23] A detailed discussion of tender offers is found in Part III.

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new company, formed by the coalition or amalgamation of the companies previously existing. (*Id., citing State ex. Rel. Nolan v. Montano R. Co.,* 21 PAC. REP. 623.)

[14] Villanueva, *supra* note 5, at 607.

[15] *Id.*

[16] Campos, *supra* note 4, at 441.

[17] *Id., citing* Pindlas Ice and Cold Storage Co. v. Commissioner, 57 F. 2d. 188.

[18] *Id.*

[19] *Id.*

[20] *Id.*

[21] Patrick Gaughan, MERGERS WHAT CAN GO WRONG AND HOW TO PREVENT IT 14 (2005).

[22] *Id.*

[23] *Id.* at 16.

Another alternative to a tender offer is a proxy contest. This is where the bidder tries to use the corporate democracy process to garner enough votes to throw out the current board of directors and the managers they have selected.[24]

III. HOW TO REPLY TO TAKEOVERS

A. TAKEOVER BID REGULATIONS

1. Acquisition of a Substantial Shareholding

Section 18 of the Philippine Securities Regulation Code (SRC)[25] provides that any person who acquires directly or indirectly the beneficial ownership of more than 5% of any class of equity security of a public company is required to disclose the acquisition to the:

- public company;[26]
- Securities and Exchange Commission (SEC); and
- Philippine Stock Exchange (PSE), if the equity security is listed.

SRC Section 18 is aimed at alerting existing stockholders and management to a possible threat of control or an impending offer.[27] Thus, SRC Subsection 18.1(b) requires information as to whether or not "the purpose of the purchases or prospective purchases is to acquire control of the business of the issuer of the securities."

This disclosure shall be made within five (5) business days after the date of acquisition of direct or indirect beneficial ownership.[28] Thereafter,

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[24] *Id.* at 17.

[25] Rep. Act No. 8799.

[26] A public company pertains to any of the following:

- An issuer whose securities are registered with the SEC;
- An issuer whose securities are listed for trading in the PSE; and
- An issuer with assets of at least P50 million or such other amount as the SEC shall prescribe, and which has 200 or more holders, each holding at least 100 shares. [(Amended Implementing Rules and Regulations of the SRC hereinafter referred to as SRC Rule 3(M)]

[27] Rafael Morales, THE PHILIPPINE SECURITIES REGULATION CODE ANNOTATED 144 (2005).

[28] SRC Rule 18.1, ¶ 2.

SRC Section 18.2 requires the purchaser to file regular reports in prescribed forms with the issuer, the SEC and the PSE (if the equity security is listed) indicating any change in the beneficial ownership[29] of the equity security.

2. Proxy[30] Solicitation

In the area of proxy solicitation, the thrust is to foster and facilitate democracy in public companies by requiring an extensive disclosure of information to the stockholders, in the form of an "information statement" (SEC FORM 20-IS) and a management report.[31] This is aimed at enabling the stockholders to make an informed decision on whom to give their proxies.

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[29] Beneficial owner or beneficial ownership means any person who, directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise, has or shares voting power, which includes the power to vote, or to direct the voting of such security; and / or investment returns or power, which includes the power to dispose of, or direct the disposition of such security; provided however, that a person shall be deemed to have an indirect beneficial ownership interest in any security which is:

1. Held by members of his immediate family sharing the same household;
2. Held by a partnership in which he is a general partner;
3. Held by a corporation of which he is a controlling shareholder; or
4. Subject to any contract, arrangement or understanding which gives him voting power or investment power with respect to such securities; provided however, that the following persons or institutions shall not be deemed to be beneficial owners of securities held by them for the benefit of third parties or in customer or fiduciary accounts in the ordinary course of business, so long as such shares were acquired by such persons or institutions without the purpose or effect of changing or influencing control of the issuer:
    a. A broker dealer;
    b. An investment house registered under the Investment Houses Law;
    c. A bank authorized to operate as such by the *Bangko Sentral ng Pilipinas* (Central Bank of the Philippines);
    d. An insurance company subject to the supervision of the Office of the Insurance Commission;
    e. An investment company registered under the Investment Company Act;
    f. A pension plan subject to regulation and supervision by the Bureau of Internal Revenue and / or the Office of the Insurance Commission or relevant authority; and
    g. A group in which all of the members are persons specified above.

All securities of the same class beneficially owned by a person, regardless of the form such beneficial ownership takes, shall be aggregated in calculating the number of shares beneficially owned by such person. A person shall be deemed to be the beneficial owner of a security if that person has the right to acquire beneficial ownership, within thirty (30) days, including, but not limited to, any right to acquire, through the exercise of any option, warrant or right; through the conversion of any security; pursuant to the power to revoke a trust, discretionary account or similar arrangement; or pursuant to automatic termination of a trust, discretionary account or similar arrangement. [SRC Rule 3(A)].

[30] A proxy is a contract of agency between a stockholder (as principal) and the proxyholder (as the agent) through which the physical absence of an individual stockholder at a stockholders' meeting is transformed into a juridical or legal presence. (Morales, *supra* note 27, at 168).

[31] Morales, *supra* note 27, at 152.

3. Protection of Shareholder Interest

The Securities Regulation Code (SRC) provides for stringent rules for tender offers to protect minority shareholders whose shares are often not taken up by a take-over group. The term "tender offer" means a publicly announced intention by a person acting alone or in concert with other persons to acquire equity securities of a public company.[32]

The tender offer rules seek to establish standards for the dissemination of a tender offer and for the pro-rating of an acquisition in the event that the securities tendered are more than the number desired by the purchaser. The tender offer rules also seek to protect the shareholders of public companies by ensuring equal access to the tender offer and fair treatment of all shareholders who wish to tender their securities.

If the tender offer shall be for less than the total outstanding securities of a class but a greater number of securities is tendered pursuant thereto, the bidder shall be bound to take up and pay for the securities on a *pro rata* basis, disregarding fractions, according to the number of securities tendered by each security holder during the period such offer remains open.[33]

4. Mandatory tender offers

Under the SRC Rules,[34] a purchaser is required to make a tender offer for equity of shares of a public company in an amount equal to the number of shares that the person intends to acquire in the following circumstances:

- Purchaser intends to acquire 35% or more of the equity shares in one or more transactions within a period of twelve (12) months;[35] or

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[32] SECURITIES REGULATION CODE, Rule 19(1).

[33] SECURITIES REGULATION CODE, Rule 19, ¶ 9(E).

[34] SECURITIES REGULATION CODE, Rule 19(2) and (3).

[35] A. Any person or group of persons acting in concert, who intends to acquire thirty-five percent (35%) or more of equity shares in a public company shall disclose such intention and contemporaneously make a tender offer for the percent sought to all holders of such class, subject to paragraph (9)(E) of this Rule.

• If the acquisition would result in ownership of 51% or more of the equity shares of a public company.[36]

Pursuant to paragraph 3 of SRC Rule 19, a purchaser is exempted from the requirement to make a mandatory tender offer in the following circumstances:

• Purchase of newly issued shares from unissued capital stock, provided the acquisition will not result to a 50% or more ownership of the shares by the purchaser;

• Any purchase of shares from an increase in authorized capital stock;

• In connection with foreclosure proceeding involving a duly constituted pledge or security arrangement where the acquisition is made by the debtor or creditor;

• Purchases in connection with privatization undertaken by the government of the Philippines;

• Purchases in connection with corporate rehabilitation under court supervision;

• Purchases through the open market at the prevailing market price;

• Merger or consolidation.

In the event that the tender offer is oversubscribed, the aggregate amount of securities to be acquired at the close of such tender offer shall be proportionately distributed across both selling shareholders with whom the acquirer may have been in private negotiations and minority shareholders [SECURITIES REGULATION CODE, Rule 19(2)(A)].

B. Any person or group of persons acting in concert , who intends to acquire thirty-five percent (35%) or more of equity shares in a public company in one or more transactions within a period of twelve (12) months, shall be required to make a tender offer to all holders of such class for the number of shares so acquired with the said period [SECURITIES REGULATION CODE, Rule 19(2)(B)].

[36] If any acquisition of even less than thirty-five percent (35%) would result in ownership of over fifty-one percent (51%) of the total outstanding equity securities of a public company, the acquirer shall be required to make a tender offer under this Rule for all the outstanding equity securities to all remaining stockholders of the said company at a price supported by a fairness opinion provided by an independent financial advisor or equivalent third party. The acquirer in such a tender offer shall be required to accept any and all securities thus tendered.

Purchasers exempt from mandatory tender offer are nonetheless required to comply with disclosure requirements and other obligations imposed by the SRC.

5. Announcements

Any person making a tender offer shall make an announcement of his intention in a newspaper of general circulation, prior to the commencement of the offer.[37] However, such announcement shall not be made until the purchaser has the resources to implement the offer in full.[38]

A purchaser wishing to make a tender offer for a class of securities of a public company is required to file a tender offer statement together with the tender offer materials with the SEC, the public company, and the PSE (if the equity securities are listed), at least two (2) business days prior to the commencement of the tender offer.[39]

On the commencement date of the tender offer and for two (2) consecutive days thereafter, the purchaser is also required to publish, send or give the tender offer to the security holders by complying fully with either of two methods of dissemination of the tender offer: long form publication or summary publication.[40]

If a person becomes aware of a potential tender offer before such offer has been publicly announced, that person may not buy or sell, directly or indirectly, the securities of the public company that is the target of the

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[37] SECURITIES REGULATION CODE, Rule 19, ¶ 5.

[38] *Id.*

[39] *Id.*

[40] 8. Dissemination Requirements

A. A bidder or an issuer shall disseminate the tender offer by complying fully with one of the following methods of dissemination:

i. Long Form Publication. The bidder shall publish in two (2) newspapers of general circulation in the Philippines on the date of commencement of tender offer and for two (2) consecutive days thereafter the information required by paragraph 7(A) of this Rule.

ii. Summary Publication. The bidder shall publish in two (2) general newspapers of general circulation in the Philippines on the date of commencement of the tender offer and for two (2) consecutive days thereafter the information required by paragraph 7(A)(i) through (viii) of this Rule, including appropriate instructions for security holders on how to obtain promptly, at the expense of the bidder, the information included in SEC Form 19-1, and furnish promptly a copy of such form to any security holder who requests a copy of such information (SECURITIES REGULATION CODE, Rule 19, ¶ 8).

potential tender offer until the tender offer is publicly announced. Such buying or selling constitutes insider trading under the SRC.[41]

6. Timetable

Unless withdrawn, a tender offer must remain open for at least twenty (20) business days from its commencement.[42] In case of an amendment in the percentage of the securities or in the tender offer price, the tender offer must remain open for at least ten (10) business days from the date of notice of the amendment.[43]

The purchaser may extend the length of the tender offer by issuing a notice of extension by press release or by other public announcement no later than the scheduled original expiration date of the offer.[44] The notice of extension must disclose the approximate number of securities tendered to date.[45] Any security tendered may be withdrawn by the security holder at any time during the period when the tender offer remains open or at any time after sixty (60) business days from the commencement of the tender offer if the securities are not yet accepted for payment.[46]

Except with the consent of the SEC, where an offer has been withdrawn, the purchaser or any person who acted in concert with him in the course of the offer cannot announce a new offer for the public company within six (6) months from the time the initial offer was withdrawn.[47] Neither can they acquire any of its equity securities that will obligate the purchasers to make a mandatory tender offer.[48]

The bidder in a tender offer shall either pay the consideration offered, or return the tendered securities, not later than ten (10) business days after the termination or the withdrawal of the tender offer.[49]

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[41] SECURITIES REGULATION CODE, Rule 19, ¶ 10.
[42] SECURITIES REGULATION CODE, Rule 19, ¶ 9.
[43] *Id.*
[44] SECURITIES REGULATION CODE Rule 19, ¶ 9(I).
[45] *Id.*
[46] SECURITIES REGULATION CODE, Rule 19, ¶ 9(D).
[47] SECURITIES REGULATION CODE, Rule 19, ¶ 11.
[48] *Id.*
[49] SECURITIES REGULATION CODE, Rule 9, ¶ 9(G).

B. ANTI-TAKEOVER MEASURES

In the Philippines, corporations usually employ two types of takeover defenses, namely, preventive takeover defenses and active takeover defenses.

Preventive takeover defenses are put in place in advance of any specific takeover bid. They are installed so that a bidder will not attempt a takeover.

Active takeover defenses are deployed in the midst of a takeover battle where a bidder has made an offer for the company.

1. **Preventive takeover defenses.** Examples of preventive takeover defenses are:

> a. **Poison Pill.** A poison pill typically grants shareholders the right to buy more shares at a lower price in the event of a hostile bid, making any takeover attempt more expensive and time-consuming. The Philippine Long Distance Telephone Company (PLDT), the Philippine's largest telecommunications company has armed itself with a poison pill against a possible hostile takeover. A hostile bid would automatically trigger a rights offering. This would allow all shareholders - except the raider - to buy new shares at half the market price. Triggers were also fixed. The rights offer would trigger when any investor acquires 10 % or more of the company's shares or makes an offer to acquire 10 %, or when an existing shareholder raises his stake by 5 %. This would have made it expensive for a prospective raider to acquire management control.
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> b. **Shareholders' Buy-out Agreement.** Example is the shareholders' agreement between the two largest shareholders of San Miguel Corporation, Southeast Asia's largest food and beverage group, Eduardo Cojuangco, Jr. and Kirin Brewery Company, Ltd. of Japan, which includes a buy-out clause that gives Cojuangco first right to buy shares of the Japanese firm should it sell out after five years.
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> c. **Defensive by-law provision.** A by-law provision which disqualifies any stockholder engaged in any business that competes with or is antagonistic to that of the corporation from being

nominated or elected to the Board of Directors. This kind of anti-takeover measure is also found in the by-laws of San Miguel Corporation.

d. **Dual capitalization.** These feature different classes of stock, which afford different voting rights and dividend entitlements to holders of the shares. They often involve one class of super voting rights stock, which usually pay very low dividends. These shares are usually distributed to all shareholders, but those who are interested in augmenting their control, such as managers, may retain it while others may accept a follow-up offer by the company to exchange these shares for regular voting and dividend-paying stock. The end result of such a stock offering/dividend distribution is that increased control is concentrated in the hands of shareholders who typically are more "loyal" to the corporation and who would be less likely to accept an offer from a hostile takeover.

e. **Supermajority requirement.** The requirement for supermajority approval of changes in corporate form, by-laws and articles of incorporation amendments or changes, and removal of a director. Take note, however, that the supermajority provision would not absolutely block a takeover attempt, especially by a bidder willing to buy all the target stock.[50]

f. **Golden parachutes.** "Golden parachutes" are contractual arrangements with the managers whereby very large increases in their compensation will be triggered by a successful takeover bid.[51] Golden parachutes have the effect of increasing the cost of a takeover but are defended as creating a parity of interest between shareholders and management, which allows management to act objectively in the face of a hostile takeover bid.

g. **Staggering the terms for the directors.** A staggered board alters the elections of directors so that only a limited number of directors, such as one-third, come up for election at one time. If only one-third of the board could be elected at one time then new controlling shareholders would have to wait for two elections

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[50] Clark, CORPORATE LAW 573, 576 (1986).
[51] *Id.* at 577.

before winning control of the board. This is being done in several corporations in the Philippines.

2. **Active takeover defenses.** With regard to active takeover defenses, directors have the option to implement any number of defensive techniques designed to slow or prevent the success of a tender offer that has already been made. They include:

a. **Litigation.** The filing of litigation on various grounds.[52] Unless there are important legal issues a target company can argue, this often is not enough to stop a takeover. It may, however, provide time, which may enable the target to mount other defenses.

b. **Share manipulation.** Steps to prevent changes of control such as selling large blocks of stocks to a friendly party[53] or the "buy back" of stock by the target.[54]

c. **White Knight.** A search can be conducted for a "white knight." A "white knight" is a third party, friendly to target management, which rescues the target from a hostile takeover by either entering into a friendly merger with the target or assisting the target in a defensive tactic such as a crown jewel option. "Crown jewel options" are options granted by a target to a third party to purchase the targets most valuable assets in order to discourage a hostile bidder from acquiring the target.

IV. REVIEW OF ANTI-TAKEOVER MEASURES

Indeed, with the rise of hostile takeovers comes the arrival of anti-takeover defenses in the Philippine corporate system. With this arrival comes the inevitability of litigation regarding the legality of anti-takeover defense measures.

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[52] In the United States, claims under the federal securities laws and the antitrust laws are the staples of this kind of defense mechanism.

[53] The target might sell stock to friendly entities that can be trusted not to tender to the hostile bidder, thus making it harder for the bidder to buy enough shares to make a controlling percentage. (Clark, *supra* note 50, at 573).

[54] If the incumbent controlling stockholders held a substantial block of stock, the target might offer to repurchase some of its own stock from other shareholders. If such a repurchase were large enough, it would result in the incumbent group's getting *de jure* voting control.

As a result of their strong desire to protect themselves from termination following a hostile takeover, top executives may face a conflict of interest with the corporation's stockholders. A hostile takeover presents management with a choice between risking their jobs by giving stockholders an opportunity to tender their shares for a profit or retaining their control by denying shareholders this profit.[55]

In light of this conflict of interest, the directors will find it very difficult to remain purely objective in their decision-making.[56] Self-interest of directors may naturally be intertwined with hostile takeover transactions where loss of corporate executive jobs may be a consequence of the takeover. It is in these cases where courts may be called upon to rule on the validity of anti-takeover measures. It is interesting to note that the Philippine courts have had no occasion to rule on the legality of anti-takeover measures. How will Philippine courts rule on the legal issues involved in hostile takeover scenarios?

A. AMERICAN JURISPRUDENCE

Considering that Philippine corporate law is of American origin, American jurisprudence has persuasive effect in Philippine jurisdiction. More specifically, our courts will cite the landmark cases decided by the Delaware[57] Supreme Court on hostile takeovers.

1. *Cheff vs. Mathes*, 199 2Ad 548 (Delaware 1964) – Proper Purpose Test

In *Cheff vs. Mathes*, the issue before the court was whether or not the directors, by purchasing company stock with corporate funds, had breached their fiduciary duties to the target company. The court upheld the anti-takeover measure adopted by the board saying that for as long as the board of directors can show that the entrenchment of the board of directors was not the motive for the defense, the defensive measure will not

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[55] Jonathan Roque Glinoga, DIRECTOR LIABILITY IN A HOSTILE TAKEOVER SCENARIO: FINDING A MIDDLE GROUND BETWEEN THE BUSINESS JUDGMENT RULE AND THE FIDUCIARY DUTIES OWED TO THE STOCKHOLDERS 27 (2001).

[56] *Id.*

[57] http://www.state.de.us/corp/default.shtml. The State of Delaware has the most experience in terms of hostile takeover cases in the United States. Delaware is arguably the most important state in terms of U.S. corporate law. More than half a million business entities have their legal home in Delaware including more than 50% of all U.S. publicly-traded companies and 58% of the Fortune 500.

be invalidated. According to the court "if the actions of the board were motivated by a sincere belief that the buying out of the dissident stockholder was necessary to maintain what the board believed to be proper business practices, the board will not be held liable for such decision."[58]

2. *Unocal vs. Mesa Petroleum Co.*, 493 A 2d 946 (Delaware 1985)[59] – Enhanced judicial scrutiny – threat and proportionality test

Unocal introduced the doctrine of enhanced judicial scrutiny "because of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders, there is an enhanced duty which calls for judicial examination at the threshold before the protections of the business judgment rule may be conferred.[60]

In *Unocal*, the court recognized the inherent danger in the purchase of shares with corporate funds to remove a threat to corporate policy when a threat to control is involved. The directors are of necessity confronted with a conflict of interest, and an objective decision is difficult.[61]

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[58] Cheff, 199 2Ad at 554. The facts of this case showed that Mr. Maremont, as CEO of Motor Products, was going to make substantial changes to the distribution policies of Holland Furnace. Because the board was able to point to its interest to continue the longstanding distribution policies of Holland and conducted a reasonable investigation, they were able to show that their purpose was not one of perpetuation.

[59] The facts of this case shows that Mesa, the owner of approximately 13% of Unocal's stock, commenced a two-tier "front-loaded" cash tender offer for 64 million shares, or approximately 37%, of Unocal's outstanding stock at price of $54 per share. The "back-end" was designed to eliminate the remaining publicly held shares by an exchange of securities purportedly worth $54 per share. Mesa issued a supplemental proxy statement to Unocal's stockholders disclosing that the securities offered in the second-step merger would be highly subordinated, and that Unocal's capitalization would differ significantly from its present structure. Unocal has rather aptly termed such securities "junk bonds".

Unocal's board consists of eight independent outside directors and six insiders held several lengthy board meetings, listened to detailed presentations made by legal counsel, investment bankers and appropriate company officers and deliberated about the proper action. The board decided to reject Mesa's offer. An exchange offer was made as a defense measure. The board resolution provided that if Mesa acquired 64 million shares of Unocal stock through its own offer (the Mesa Purchase Condition), Unocal would buy the remaining 49% outstanding for an exchange of debt securities having an aggregate par value of $72 per share. The board resolution also stated that the offer would be subject to other conditions that had been described to the board at the meeting, or which were deemed necessary by Unocal's officers, including the exclusion of Mesa from the proposal (the Mesa Exclusion). It is this exclusionary feature that was the focus of the court's opinion.

[60] Unocal, 493 A 2d at 954.

[61] *Id.* at 955.

In the face of this inherent conflict, directors must show that they had reasonable grounds for believing that a danger to corporate policy and effectiveness existed because of another person's stock ownership.[62] However, they satisfy that burden "by showing good faith and reasonable investigation . . ."[63]

A further aspect, said the court, is the element of balance.[64] If a defensive measure is to come within the ambit of the business judgment rule, it must be reasonable in relation to the threat posed.[65] This entails an analysis by the directors of the nature of the takeover bid and its effect on the corporate enterprise. Examples of such concerns may include: inadequacy of the price offered, nature and timing of the offer, questions of illegality, the impact on "constituencies" other than shareholders (i.e., creditors, customers, employees, and perhaps even the community generally), the risk of non-consummation, and the quality of securities being offered in the exchange.[66]

In *Unocal*, the specific threat posed was viewed by the Unocal board as a grossly inadequate two-tiered coercive tender offer coupled with the threat of greenmail, posed by an offeror whom the court characterized as a "corporate raider" with a "national reputation as a `greenmailer.'"[67]

In concluding, the court held that there was directorial power to oppose the tender offer and to undertake a selective stock exchange made in good faith and upon a reasonable investigation pursuant to a clear duty to protect the corporate enterprise. Further, the selective stock repurchase plan chosen was deemed reasonable in relation to the threat that the board rationally and reasonably believed was posed by the inadequate and coercive two-tiered tender offer. The court said:

> Under those circumstances the board's action is entitled to be measured by the standards of the business judgment rule. Thus, unless it is shown by a preponderance of the evidence that the directors' decisions were primarily based on perpetuating themselves in office, or some other breach of fiduciary duty such

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[62] *Id., citing* Cheff v. Mathes, 199 A 2d at 554-55.
[63] *Id., citing* Cheff v. Mathes, 199 A 2d at 555.
[64] *Id.*
[65] *Id.*
[66] *Id.*
[67] *Id.* at 956.

> as fraud, overreaching, lack of good faith, or being uninformed, a Court will not substitute its judgment for that of the board.[68]

3. *Revlon, Inc. vs. MacAndrews & Forbes Holdings*, 506 A 2d 173 (Delaware 1986)[69] – Revlon duty - seeking the best price reasonably available

In *Revlon*, the Delaware Supreme Court held that the decision of a board of directors permitting management to negotiate a merger or buyout with a third party was a recognition that the company was for sale. The duty of the board thus changed from the preservation of Revlon as a corporate entity to the maximization of the company's value at a sale for the stockholders' benefit. The court further said:

> [T]his significantly altered the board's responsibilities under the Unocal standards. It no longer faced threats to corporate policy and effectiveness, or to the stockholders' interests, from a grossly inadequate bid. The whole question of defensive measures became moot. The directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company.[70]

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[68] *Id.* at 958.

[69] In this case, Pantry Pride commenced a highly leveraged tender offer for 100% of Revlon at $47.50 per share. This offer was rejected by Revlon's board. As a defensive measure, Revlon commenced an exchange offer by purchasing ten million of its own shares for notes and preferred stock. The notes were a defensive device because they contained covenants that limited the company's ability to incur additional debt, sell assets, or pay dividends. As a consequence, the notes impeded any highly leveraged offer for control of the company. After Pantry Pride raised its offer to $53 per share, the Revlon board commenced an auction. Forstmann Little emerged as Pantry Pride's chief competitor and the Revlon board's preferred suitor. After Pantry pride raised its offer to $56.25, the Revlon board enticed Forstmann Little to make a $57.25 bid by agreeing to an asset lock-up option, a no-shop provision, and a cancellation fee. Forstmann Little agreed to support the value of the notes that were created by the exchange offer, which had fallen in value upon an announcement that the Revlon board intended to waive the note covenants. Pantry Pride raised its offer to $58 per share and conditioned its offer on nullification of the favoritism shown to Forstmann Little. Pantry Pride brought suit to enjoin the defensive actions taken (lock-up option, no-shop provision, and the cancellation fee). The Revlon board defended their actions on two grounds: (a) the board was entitled to advance the interests of the noteholders even if there was a small dimunition in shareholder value; and (b) the concessions granted to Forstmann Little were reasonably designed to maximize shareholder value by generating a $1 increase in the bidding. The Delaware Supreme Court invalidated the lock-up option, no-shop clause, and cancellation fee and rejected both arguments (Glinoga, *supra* note 55, at 49-50).

[70] Revlon, Inc. vs. MacAndrews & Forbes Holdings, 506 A 2d 173, 182 (Delaware 1986).

There are a lot of cases decided by the Delaware Supreme Court on hostile takeovers. The subsequent cases, however, are merely reiterations of the principles laid down in these landmark cases.

B. JAPANESE RESPONSE

1. Jurisprudence

One of the most highly celebrated takeover cases in Japan is the recent case of *Livedoor*.[71] In this case, the court ruled on the issue of when it is permissible for a target's board of directors to erect a virtually impenetrable barrier to an unsolicited bid.[72] In invalidating the defensive measure, the District Court noted the preclusive nature of Nippon Broadcasting's warrant issuance, echoing Delaware jurisprudence.[73] On

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[71] Nippon Hoso K.K. v. Livedoor K.K., Appeal from Preliminary Injunction Against Issuance of Warrants, Tokyo High Court, March 23, 2005. Background. On January 17, 2005, Fuji Television Network, Inc. (Fuji) announced an all cash tender offer at ¥5,950 for all the outstanding shares of Nippon Broadcasting System, Inc. (NBS), which offer had a minimum share tender condition of 12,333,341 (which number of shares when added to the 4,064,000 shares already owned by Fuji, would give it slightly over 50% of the outstanding shares). On February 8, 2005, Livedoor Co., Ltd. (Livedoor) announced that it had purchased approximately 29.6% of NBS's outstanding shares, which, in combination with the shares already held by it, gave it 35.15% OF NBS's outstanding shares. Livedoor also indicated in this announcement an intent to seek majority control of NBS, and subsequently has purchased additional shares and now owns an estimated 40.5% of NBS's shares. In response, the market price of NBS shares rose to ¥6,500 and has subsequently traded at even higher levels, most recently at or around ¥6,700.

Next, on February 15, 2005, Fuji amended its tender offer, cutting back the minimum number of shares to be purchased to 4,135,341 (which, combined with its existing ownership in the NBS, would give it slightly more than 25% of NBS). Then on February 23, 2005, NBS and Fuji announced at a joint press conference that the NBS board had decided to issue warrants to Fuji giving the latter the right to purchase 47.2 million NBS shares. This number of shares comes to approximately 140 percent of the number of currently outstanding NBS shares, and such an issuance would both give Fuji majority control and dilute Livedoor's ownership percentage to less than 20%. The warrants are exercisable at ¥5,950 (the identical price to that offered by Fuji in its tender offer but well below the current market price), and they are redeemable by NBS at any time prior to Fuji's exercise of them. NBS further announced that its purpose for the warrant issuance was (a) to prevent Livedoor from acquiring control and (b) to remain within the Fuji group because of the long-term benefits from such an association to its shareholders. (Background was lifted verbatim from the opinion of John C. Coffee Jr., filed with the Tokyo District Court Civil Dept. No. 8, March 8, 2005, pages 2-3 published in Kigyo Baishu wo Meguru Shosou to Nippon Housou Jiken Kantei Iken Bessatsu Shoji Houmu No. 289, Shouji Houmu Kenkyu Kai, August 23, 2005).

[72] Curtis Milhaupt, *In the Shadows of Delaware? The Rise of Hostile Takeovers in Japan*, Working Paper No. 278, Columbia Law School, the Center for Law and Economic Studies, Aug. 1, 2005 at 33.

[73] *Id.*

appeal, the High Court affirmed the District's Court's decision, explaining its decision as follows:

> In principle, where a contest for corporate control has merged, it constitutes a grossly unfair issuance (Commercial Code §280-39(4); §280-10) to issue warrants, the primary purpose of which is for existing management or a specific shareholder who exercises influence over management to retain control, by diluting the holdings of another shareholder. However, where the hostile bidder (1) intends to make a target company or its affiliates repurchase the shares for a premium after the stock price increases (is engaged in greenmail); (2) intends to transfer intellectual property, know how, corporate secrets, key business transactions or customers, which are vital for the management of the company, to the bidder or its affiliates (is engaged in "scorched earth" policies); (3) has acquired the target company's shares so that after acquiring control, the bidder can liquidate assets to secure or pay off bidder's debts or those of related companies; or (4) obtains temporary control of management to sell off valuable assets unrelated to the core business such as real estate or securities in order to pay a one-time dividend from the proceeds, or sell the stock after having driven up the stock price due to the high dividend---in other words, where there is an abusive motive of exploiting the target---then it is not appropriate to protect the bidder as a shareholder, and if it is clear that the interests of other shareholders will be harmed, issuance of warrants may be permitted as appropriate in order to preserve or protect management's control rights, within the limits of necessity and appropriateness as to method of resistance.[74]

Another case is the *Nireco* case wherein the Tokyo District Court rejected the petition of Nireco Corporation (a Tokyo-based control- and measuring-equipment maker, hereinafter referred to as Nireco for brevity) to revoke an injunction against the company implementing what was to be Japan's first poison pill measure.[75] This ruling confirmed the court order issued by the same court on June 1, 2005[76] in response to an injunction

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[74] Milhaupt, *supra* note 72, *citing* Nippon Hoso K.K. v. Livedoor K.K. at 56.

[75] Tokyo District Court, Jun. 9, 2005.

[76] In the earlier ruling against the poison pill, the district court said Nireco's measure, adopted by its board in March – a first in Japan – "carries the danger of inflicting unexpected damage to shareholders."

request filed by SFP Value Realization Master Fund Ltd., a Cayman Islands-based investment fund and Nireco shareholder, to prevent Nireco from issuing free stock subscription warrants to all shareholders in the event of an unwelcome takeover bid.

Nireco had planned to issue warrants to shareholders of record as of March 31 so they could buy up to two Nireco shares at 1 yen each for every share owned.[77] If all the shareholders exercised the warrants, the number of outstanding Nireco shares would triple, diluting the percentage of shares held by a firm attempting a takeover.[78]

In handing down the June 9 ruling, the court said that companies need to "proceed cautiously" in the event they want to issue new share warrants that could seriously hurt shareholders. Such a move must reflect the will of the shareholders expressed in the annual general meeting and cannot simply be endorsed by the company board, as in Nireco's case, the court said. But the court also said, "Warrants for new share issues can be issued by a company's board as an emergency measure when there is some dispute (as to) who has the right to control management (as a result of a takeover), as there would be no time to seek the opinions of shareholders."

In *Japan Engineering Consultants Co., Ltd. (JEC)*[79], the court rejected Yumeshin Holding Co., Ltd.'s motion for injunction to halt the stock split planned by JEC. The Tokyo District Court ruled that JEC could execute a stock split to protect itself from a hostile takeover bid by Yumeshin Holdings Co. The court ruled that Japan Engineering's 5-for-1 stock split should be allowed as it had "no intent to defend the management's own interests" and would not change existing shareholders' rights.

It is interesting to note, however, that although the court rejected Yumeshin's motion for injunction, it went on to say that "there is reason to doubt the suitability of the stock split as a means of resistance in the event that the split results in a significant obstacle to execution of this tender offer." In addition, the court said that in the event that Yumeshin sustains

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[77] Japan Times, Jun. 10, 2005, *available at* http://search.japantimes.co.jp/print/business/nb06-2005/nb20050610a2.htm.

[78] *Id.*

[79] Yumeshin Holdings Co., Ltd. v. Japan Engineering Consultants Co., Ltd. (JEC), Motion Requesting an Injuction to Halt the Stock Split Planned by JEC, Tokyo District Court, Jul. 29, 2005.

damages following the stock split, "Yumeshin should begin legal proceedings against the directors who approved the stock split resolution for compensation for damages under Article 266-3 of the Commercial Code of Japan.)

These rulings generated judicial standards for review of the most common defensive measure in Japan that has been aptly described as a kind of Unocal rule with Japanese characteristics.[80]

2. Ministry of Economy, Trade and Industry (METI) Takeover Guidelines

METI established a Corporate Value Study Group[81] to identify fair defensive measures against hostile takeover that would also promote corporate value. Building upon the final report of the Study Group entitled "Report on Corporate Value," the METI and the Ministry of Justice jointly released "Guidelines Regarding Takeover Defense for the Purposes of Protection and Enhancement of Corporate Value and Shareholders' Common Interests" on May 27, 2005. Although the guidelines are not legally binding, they present legally valid and reasonable criteria for the adoption of defensive measures against hostile takeover under the three principles of (i) protecting and enhancing corporate value and the interests of shareholders as a whole, (ii) prior public disclosure and shareholders' consent, and (iii) ensuring the necessity and reasonableness of defensive measures.

According to the report, the ultimate test is whether or not the defensive measures enhance corporate value. In judging the reasonableness of defensive measures, it is important to demonstrate the following: (1) that a threat to corporate value exists; (2) that the defensive measure adopted are

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[80] Milhaupt, *supra* note 72.

[81] The Corporate Value Study Group were guided by the following principles:

- enhancement of corporate value;
- equal footing with global standards;
- no discrimination between foreign and domestic companies; and
- offering increased options for shareholders and management

It is believed that by adopting Western style defensive measures, Japanese management will have more time and increased leverage to negotiate with hostile suitors. (Kigyo Kachi Kenkyu Kai (Corporate Value Study Group), Tekitaiteki Baishu Boei Saku (Kigyo Kachi Boei Saku) no Seibi [Preparing Defensive Measures toward Hostile Takeovers (Measures to Defend Corporate Value)], March 2005. (Hereinafter Interim Report), at 5, *available at* http://www.meti.go.jp/english/information/downloadfiles/Corporate%20Value.pdf).

not excessive but instead proportionate to the threat; and (3) the decision to adopt (or apply) the defensive measures is taken by the board in an "independent" manner.

In explaining the existence of threat to corporate value, the group's Interim Report[82] cited the following examples of threats:

> (1) Structurally coercive hostile takeover, for example, when the bidder is a "green mailer"
>
> (1) Practically coercive hostile takeover, for instance, when shareholder who do not have enough information accept the under priced offer, thus, the opportunity to receive the company's long-term value will be lost.
>
> (3) Acquisition proposal which does not allow the target's board enough time to consider alternative plans, such as when a bidder launches a tender offer bid without any prior notice and the target's management does not have enough time to consider alternative plans.

In elucidating the proportionality test, the Interim Report[83] said:

> (1) The defensive measures do not take away shareholders' fundamental right to choose. The avenue for proxy contest must be preserved. Shareholders must have the ability to change directors at a general shareholders' meeting to eliminate the defensive measures, if they so choose.
>
> (2) Redemption standard of defensive measures has to be reasonable. The following are key factors for consideration:
>
> > (a) Prior disclosure of redemption standard.
> >
> > (b) Existence of a third party check
> >
> > (c) Objectivity of redemption terms; and

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[82] *Id.* at 8.
[83] *Id.*

(d) Prior approval of shareholders

In explaining independent decision making process, the following are the key factors for consideration, according to the Interim Report[84]:

(1) The target's board of directors must carry out good faith and reasonable investigation of the hostile bid relative to the stand-alone strategy.

(2) It is better for the board to seek the advice from experts and independent third parties.

(3) It is better to involve independent third parties in determining the degree of the threat and the defensive measures taken.

(4) Prior shareholder approval could enhance the reasonableness of the decision making process.

V. QUO VADIS, PHILIPPINES? HOW DO WE REPLY TO ANTI-TAKEOVER MEASURES?

A. BUSINESS JUDGMENT RULE

Philippine courts will definitely be guided by the business judgment rule.[85] The corporate principle recognizing corporate power and competence to be within the board of directors is embodied in the "business judgment rule." It is a well known rule of law that questions of policy or of management are left solely to the honest decision of officers and directors of a corporation, and that the courts are without authority to substitute its judgment for the judgment of the board of directors; the

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[84] *Id.*

[85] In Pogostin v. Rice, 480 A. 2d 619, 627 (Del. 1984), the Delaware Supreme Court held that the business judgment rule, including the standards by which director conduct is judged, is applicable in the context of a takeover.

board is the business manager of the corporation, and as long as it acts in good faith, its orders are not reviewable by the courts.[86]

Generally, courts and other administrative bodies having jurisdiction over corporations would not overturn or interfere with the judgment of business decisions of the board, nor will they substitute their wisdom for that of the board. This principle finds support under Sec. 23 of the Philippine Corporation Code, where the contract of the State with the corporation, its investors and the public at large who must deal with the corporation, is that the "corporate powers" are vested in the board.

The board of a corporation has the sole authority to determine policy and conduct the ordinary business of the corporation within the scope of its charter. The directors elected by the stockholders act as a body in the formulation of all corporate policies and exercise all powers of management, to the exclusion of stockholders.[87] If in the course of management directors arrive at a decision for which there is a reasonable basis, and they acted in good faith, as a result of their independent judgment, and uninfluenced by any consideration other than what they honestly believe to be for the best interests of the corporation, it is not the function of the court to say that it should have acted differently to charge the directors for any loss or expenditure incurred.[88] Explaining the business judgment rule, the Philippine Supreme Court said:

> It is a well-known rule that questions of policy or of management are left solely to the honest decisions of officers and directors of a corporation, and the court is without authority to substitute its judgment for the judgment of the board of directors; the board is the business manager of the corporation, and so long as it acts in good faith, its orders are not reviewable by the courts.[89]

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[86] Sales v. Securities and Exchange Commission, G.R. No. 54330, 169 SCRA 125, Jan. 13, 1989, *citing* Fletcher on Corporations, VOL. 2, at 390.

[87] Jose Campos Jr. & Maria Clara L. Campos, THE CORPORATION CODE COMMENTS, NOTES, AND SELECTED CASES, VOL. 1 at 641.

[88] *Id.* at 643, *citing* Casey v. Woodruff, 49 N.Y.S. 2d 625 (1944)

[89] Montelibano v. Bacolod-Murcia Milling Co., Inc., G.R. No. 15092, 5 SCRA 36, 42, May 18, 1962.

The problem, however, with the business judgment rule is that since target management can and do allege the corporate good as a basis for undertaking defensive measures, this rule makes it impossible to attach any but the most outrageous defensive maneuvers.[90]

B. FIDUCIARY DUTY OF DIRECTORS IN THE PHILIPPINE CORPORATE CONTEXT – DUTY OF LOYALTY, DILIGENCE AND CARE

Second, Philippine courts will be guided by the fiduciary duty of directors. Board of Directors are thus given broad powers under Philippine corporate law. In granting them these broad powers, the law in effect makes them fiduciaries of the corporation, and as such, they are expected to serve the corporation with reasonable diligence and skill with utmost loyalty to its interests.

The Philippine Corporation Code has attempted to lay down general rules of conduct and although these serve as guidelines for directors to follow, the determination as to whether in a given case the duty of loyalty has been violated has ultimately to be decided by the court on the case's own merits.[91]

The Philippine Supreme Court held that the primary obligation of the directors of a corporation is "to seek the maximum amount of profits for the corporation," and characterized the position as a "position of trust" and that in case his interests conflict with those of the corporation, he cannot sacrifice the latter to his own advantage and benefit."[92] The Court said in another case, "equity recognizes that stockholders are proprietors of the corporate interests and are ultimately the only beneficiaries thereof. . ."[93]

Corporate fiduciary duties require the directors to exercise their judgment when circumstances pose a possible threat to the best interests of

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[90] Clark, *supra* note 50, at 582.

[91] *Id.* at 687

[92] Villanueva, *supra* note 5, at 224, *citing* Prime White Cement v. Intermediate Appellate Court, G.R. No. 68555, 220 SCRA 103, 110, Mar, 19, 1993.

[93] Gokongwei v. Securities and Exchange Commission, G.R. No. 45977, 89 SCRA 336, 368, Apr. 11, 1979.

the corporation. Specifically, it is well settled that corporate directors have the duty to determine whether a tender offer or takeover bid is in the best interest of the corporation and its shareholders.[94] Where the offeror has a history of mismanaging its acquisitions or depleting its acquisitions' assets, or where the acquisition could result in debilitating litigation, directors should take defensive measure to block the takeover.[95] The situation may also arise where the offer is inadequate, unfair or otherwise detrimental to the best interests of the corporation and its shareholders.[96]

VI. RECOMMENDATIONS

Indeed, the Philippines is blessed with a unique opportunity to learn from the two largest economies in terms of dealing with the legality of anti-takeover measures in the very near future. At present, the only standard of review for takeover cases existing under Philippine corporate jurisprudence is the business judgment rule. American experience has shown, however, that under the business judgment rule, the American courts have strained to grant deference to the expertise of directors and have been unwilling to second-guess their decisions.[97] As a result, virtually any business decision can be shown to have been made in good faith and in the honest belief that it was in the best interests of the corporation.[98] To protect the interests of the shareholders, this author believes that Philippine courts should take a more critical examination of the rationales underlying decisions made by the board of directors in adopting anti-takeover measures. Thus, *Unocal's* enhanced judicial scrutiny and *Revlon's* duty of seeking the best price available should be taken into account by the Philippine courts in reviewing the legality of anti-takeover measures

It is believed that these standards should, however, be adapted to suit local interests. In practice, successful economies do not abandon their institutions for foreign models.[99] Rather, foreign legal technologies are

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[94] Glinoga, *supra* note 55, at 3.
[95] *Id.*
[96] *Id.*
[97] *Id.* at 81.
[98] *Id.*
[99] Milhaupt, *supra* note 72.

selectively adopted locally, then adapted by coalitions of market and governmental actors to suit their own interests.[100]

Guidelines on anti-takeover measures should be drawn by the Philippine Securities and Exchange Commission (SEC)[101] similar to the Takeover Guidelines adapted by the Ministry of Economy, Trade and Industry (METI). The opinion of the SEC should also be sought in cases where an interested party wants to clarify the legality of an anti-takeover measure.

This author also suggests that a special court similar to the Philippine Court of Tax Appeals,[102] a specialized court dealing with tax cases, should be established for the purpose of dealing with corporation law issues. Considering that a lot of issues in corporation law require the technical expertise of judges who are specialists in corporation law, it is essential to have a court that specializes in corporation law. The author believes that the possibility that the business judgment rule will be strained to grant deference to the expertise of directors will be reduced to a minimum if the Philippines establishes a court that has expertise in corporation law.

VII. CONCLUSION

At present, there is a lack of jurisprudence on anti-takeover litigations in the Philippines. Such a situation, I believe, presents us with a

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[100] *Id.*

[101] Under Sec. 5 of the Securities Regulation Code (Rep. Act No. 8799), the Securities and Exchange Commission (SEC) was given the power, among others, to have jurisdiction and supervision over all corporations, partnerships, or associations who are the grantees of primary franchises and/or a license or permit issued by the Government;

[102] The Court of Tax Appeals (CTA) was created under Rep. Act No. 1125. It is a special court of limited jurisdiction. Rep. Act No. 9282 expanded the jurisdiction of the CTA, elevating its rank to the level of a collegiate court with special jurisdiction and enlarging its membership. Previously, only decision, judgment, ruling, or inaction of the Commissioner of Internal Revenue, the Commissioner of Customs, the Secretary of Finance, the Secretary of Trade and Industry, or the Secretary of Agriculture, involving the National Internal Revenue Code and the Tariffs and Customs Code on civil matters are appealable to the CTA. The expanded jurisdiction transferred to the CTA the jurisdiction of the Regional Trial Courts and the Court of Appeals over matters involving criminal violation and collection of revenues under the National Internal Revenue Code and Tarriffs and Customs Code. In addition, it also acquired jurisdiction over cases involving local and real property taxes which used to be with the Regional Trial Court and the Court of Appeals.

unique opportunity to learn from countries with more advanced judicial systems such as the United States and Japan. Hopefully, the Philippines will be able to institute the proper jurisprudential rules on anti-takeover measures in the very near future. This is necessary for a stable and effective legal framework for corporations doing business in the Philippines.

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