Merger and Acquisition Law in the Age of Trump

By Carl L. Stine

The board of directors of a fictional publicly traded company, Flagco, Inc. decides to put that company up for sale. The main factory of Flagco, which makes American flags, is located in a small town in Ohio and employs 1,000 workers. In response to the sales outreach, the company receives two bids: one bid from Bidder A for $40 per share and one bid from Bidder B for $41 per share. Bidder A, a family-owned company also located in Ohio, plans to keep the factory open and keep all of the 1,000 workers; Bidder B, a Chinese consortium, based on cost-saving "synergies," plans to shut down the factory, fire all 1,000 workers, and use its factory in Mexico, which already makes Chinese flags. Although Flagco has no contacts or relationship with the state of Delaware, the company, like more than half the publicly traded corporations in the United States and 64% of Fortune 500 firms, is incorporated in Delaware.

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Under the law of Delaware, which applies because Flagco is incorporated there, the board of directors has no choice: it must accept the $41 per share bid from Bidder B. It is not permitted to even consider the fate of the 1,000 workers who will be fired or their families or the community that they live in. The directors become mere "auctioneers," required to accept the best price reasonably available. Because of the potential cost-savings of shutting down factories, bidders that can take advantage of these "synergies" can often outbid those that cannot.

Permitting a board to consider a company's other constituencies--for example, employees and the communities in which it operates—is not a radical concept. A number of states have recognized this issue and have passed what are generally referred to as "Other Constituency Statutes." Under these statutes, for example Indiana's, a director can consider "the effects of any action on shareholders, employees, suppliers, and customers of the corporation, and communities in which offices or other facilities of the corporation are located, and any other factors the director considers pertinent."

This concept is certainly not alien to ERISA plan fiduciaries. In its October 22, 2015 "Fact Sheet," the U.S. Department of Labor clarified that ESG (environmental, social, and governance) factors could, in many instances, be considered when making investment decisions.

In the age of Trump, directors and others are now faced with this tension. On the one hand, profitable mergers increase immediate compensation for a specific company's shareholders and help drive the stock market to even higher heights. On the other hand, those same mergers could mean the closing of plants and the loss of jobs in the U.S.—potentially a public relations nightmare for the parties involved, the Delaware courts, and even the administration.

It will be interesting to see whether Delaware, which is the choice of half of the corporations in this country, will be faced with this issue and whether its judges will succumb to pressure to permit directors greater latitude when considering merger options that might, in the long run, be better for the local and U.S. economy as a whole, or whether they will stick to their guns and require directors to continue to act as auctioneers. ◆

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