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OFFICIAL TRANSCRIPT
PROCEEDINGS BEFORE

THE SUPREME COURT OF THE UNITED STATES

DKT/CASE NO. 86-71 & 86-97

TITLE CTS CORPORATION, Appellant V. DYNAMICS CORPORATION OF AMERICA, ET AL.; and INDIANA, Appellant V. DYNAMICS CORPORATION OF AMERICA, ET AL.

PLACE Washington, D. C.

DATE March 2, 1987

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IN THE SUPREME COURT OF THE UNITED STATES

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CTS CORPORATION, :

Appellant :

v. : No. 86-71

DYNAMICS CORPORATION OF :

AMERICA, ET AL.; :

and :

INDIANA, :

Appellant :

v. : No. 86-97

DYNAMICS CORPORATION OF :

AMERICA, ET AL. :

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Washington, D.C.

Monday, March 2, 1987

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 11:43 a.m.

APPEARANCES:

JAMES A. STRAIN, ESQ., Indianapolis, Indiana; on behalf of Appellant CTS Corporation.

JOHN F. PRITCHARD, ESQ., New York, N.Y.; on behalf of Appellant Indiana.

LOWELL E. SACHNOFF, ESQ., Chicago, Illinois; on behalf of Appellee Dynamics Corporation of America, et al.

C O N T E N T S

P R O C E E D I N G S

(11:43 a.m.)

CHIEF JUSTICE REHNQUIST: Mr. Strain, you may proceed whenever you are ready.

ORAL ARGUMENT OF JAMES A. STRAIN

ON BEHALF OF APPELLANT CTS CORPORATION

MR. STRAIN: Mr. Chief Justice, and may it please the Court:

The principle this Court must consider in this case is the federalist intention between the power of Indiana to define the bundle of rights inherent in Indiana created corporations and the implicit limitation on that power derived from the commerce clause when Congress has not acted.

There was a different holding as well in the Seventh Circuit's opinion, and that was a pre-emption holding. But the centerpiece of that holding and DCA's argument, I might say, is that it is possible that in light of the controlled share acquisition statute under consideration today, a hostile bidder might wish to keep his tender offer open for 50 days instead of the 28-day or 20 business day minimum currently required by Rule 14(e)1 of the Securities and Exchange Commission.

Unlike the position the United States took in this Court in MITE, in this case the United States has argued that the statute is not pre-empted. Morever, the SEC has taken no exception to that position.

The SEC, indeed, is a signator on the brief in the same sense as being a part of the brief. And I might say to the Court as well, it has been suggested to me that the SEC did not join in that portion of the United States' argument but similarly there are portions of the commerce clause that only refer to the United States.

It strikes me, therefore, that the SEC disagreed. It should have said so, and it has not. The fundamental issue, then, before this Court is whether the dormant commerce clause limits the ability of Indiana to enact a statute that concededly does not discriminate between in-state and out-of-state acquirers; that unlike the statute this Court considered in MITE, does not pose any possibility of multiple and inconsistent burdens that presents no different kind of alleged burdens on interstate commerce than any number of other corporate statutes regulating the relationships inter sese among shareholders of Indiana created corporations.

QUESTION: Mr. Strain, may I inquire what you think the purpose of the statute is?

MR. STRAIN: Of course.

QUESTION: Do you think, at least in part, it is to try to keep jobs and corporate headquarters and so forth within the State of Indiana?

MR. STRAIN: No, I do not.

QUESTION: It is not a purpose at all?

MR. STRAIN: It is my belief that is not the purpose.

QUESTION: We should in making our findings and decision here conclude that that has no part for consideration in this case, is that right?

MR. STRAIN: Based on the theory that we argue, Justice O'Connor, it makes no difference.

QUESTION: Well, is it a purpose then to provide protection to stockholders of public corporations incorporated in Indiana?

MR. STRAIN: Ultimately, that has to be the purpose.

QUESTION: You think that is the purpose?

MR. STRAIN: Yes, ma'am.

QUESTION: Is it kind of a strange form of stockholder protection to in fact strip the stockholders of their right to transfer voting shares? Isn't that kind of a peculiar protection?

MR. STRAIN: Stripping the shareholders of the vote, of course, is one way to put what goes on. But it is no more peculiar, if you will, than a statute involving mergers where precisely the same result obtains.

That is that the shareholders -- that is a sufficiently important interest, at least as defined by virtually every state corporate statute of which I am aware, that the shareholders have the right to vote on whether a transaction should go forward. And if the shareholders say no, then no less in this case, somebody who lives in California who owns shares in the Indiana corporation is prevented from selling those shares one way or another to a New York based corporation located in Connecticut.

It is precisely what happens in this case.

QUESTION: Well, do you think the state could pass an outright prohibition of the transfer of voting shares in takeover bids?

MR. STRAIN: This Court squarely held in Aldridge that among the bundle of rights that the state creates is the right of transferability. The state therefore could pass a statute that ultimately says, there shall be no transfer at all of any rights in connection with the shares.

Now, it might be economically foolish to do so, and indeed I believe it would be economically foolish to do so.

QUESTION: You think there would be no commerce clause violation or concern, in any event?

MR. STRAIN: Indeed I do not. In fact, the government so argues in its argument when it tells us that it is possible to structure a corporate statute that says, there shall be no transfers when there is a possibility for someone to own more than 20 percent of the outstanding shares of the corporation.

QUESTION: May I follow up on the question -- I am over here.

MR. STRAIN: I beg your pardon, Justice Scalia.

QUESTION: Justice O'Connor asked about one of the purposes served perhaps by this statute, and other similar statutes, is to retain major corporate headquarters in a state. It certainly is a benefit to have the headquarters of a major corporation located in a state from a standpoint of employees, civic and charitable contributions, and the like.

MR. STRAIN: There is no doubt that that is --

QUESTION: You have perhaps read about the uproar down in North Carolina.

MR. STRAIN: Yes, sir.

QUESTION: Where there was some talk that R.J. Reynolds will no longer be in that state. So, why do you concede, or do you, that this is not even an objective in any way whatever, this particular statute?

MR. STRAIN: Well, I don't view what I have said as a concession. It's perfectly possible, as the State of Indiana has argued in its brief, that the shareholders of an Indiana created corporation can take those kinds of considerations into account.

But it isn't necessary, and ultimately it's the shareholders who get to decide. It's not the State of Indiana that gets to decide, which again is unlike the situation in MITE.

Remember that ultimately what occurs is that shareholders get to vote, and if the shareholders decide that they are better off with somebody from outside the state saying, we want your company, that's the way it goes.

If this is a way to preserve Indiana corporations in Indiana, it fails. One of the benefits and the burdens of the Indiana business corporation law is this statute.

Shareholders in certain limited Indiana corporations have been provided the right to vote unless they or the board of directors say otherwise, and by that of course the shareholders themselves can opt out of this kind of statute by an amendment to the articles of incorporation.

The board of directors can opt out by virtue of a by-law amendment. But in all events, if that occurs or fails to occur, then the shareholders are given the opportunity to have voting rights to determine whether someone acquires one-fifth or more, one-third or more, or one-half or more of the voting power of an Indiana corporation.

If the grant of voting power is approved, then shareholders properly exercising dissenter's rights in the same way they are granted dissenter's rights in merger transactions, can seek and obtain appraisal. The State of Indiana has concluded that this potential change in status of a shareholder is sufficiently significant that the shareholder should have a say in the outcome.

The effect of such an acquisition of control could be effectively to disenfranchise them. Take as an example, if someone acquires an excess of 50 percent of the outstanding voting power of a corporation, the remaining shareholders have utterly no vote in their future.

The United States agrees with the State of Indiana that the shareholders have a significant interest in the outcome of that kind of change of control.

CTS submits that none of DCA, the Seventh Circuit, or even the United States has identified for this Court a constitutionally cognizable line that says on the one hand, the control share acquisition statute impermissibly burdens interstate commerce and on the other hand, any of a number of statutes implicating the passing of control, such as cumulative voting rights, merger transactions, super-majority requirements for mergers, provisions for staggered boards, or even the ability to vote annually for directors or a class of directors do not.

If the Court constitutionalizes state corporate law in this case, there is no doctrinal bright line to prohibit the same result in any of a number of a long list of attributes of virtually every corporate statute that can be alleged to impede the so-called interstate market for corporate control.

Yet, these are provisions that have inhered in the corporate statutes for years without any serious question of constitutionality. If the control share acquisition statute is unconstitutional because it is different or it is new, then the states are effectively prohibited from taking into account future changes in economy.

Corporations are exclusively creatures of state law. They exist, if at all, because a given state enacted a statute allowing the corporation to come into existence, and accepted articles of incorporation that complied with that statute.

Most importantly, when anyone determines to purchase a share of stock in a corporation chartered by a state, he also buys the bundle of rights and the obligations defined by the totality of the chartering state's laws. That is and must be true whether the shares are sold exclusively intrastate or in interstate commerce.

That bundle of rights inherent in a share of stock governs everything from the value on liquidation and dissolution, the rights to dividends, if any, the ability to participate in shareholders meetings, if at all, the amount of that participation, and the kinds of issues in which participation is allowed, all the way through to whether the share of stock can be transferred as in Aldridge, and if so, under what conditions.

The very existence and nature of voting rights is solely a function of the chartering state's law, whether the share of stock is traded in interstate commerce or in intrastate commerce. Indeed, it couldn't be any other way under the decisions of this Court.

No magic transformation occurs in a share of stock when the share is placed in interstate commerce. State law, not federal law, still governs the voting rights. And to date no one has suggested, at least directly, that one share, one vote, has been imposed on the chartering state's law by the commerce clause.

Indeed, to the contrary, one only has to remember that under the common law it was the shareholder who had one vote, not vote based on the number of shares. Delaware has chartered corporations where it was possible under the articles of incorporation for a person to have declining voting rights as the share power increased.

As the United States at least recognizes, necessarily there will be so-called extraterritorial effects of the chartering state's law because the benefits and burdens constitutionally must follow the stock wherever it goes.

Thus, and pursuant to a chartering state's statutory merger procedure, the will of the majority or super-majority of the shareholders is that a merger not occur, then it will not occur even though the practical effect is to stop a New York corporation from acquiring an Indiana corporation and stopping a shareholder from California from selling -- the ability to sell shares.

Indeed, under the merger statutes, if the directors don't even submit the proposal to the shareholders at all, the shareholders never get the right to vote at all. No one, not DCA, not the Seventh Circuit, not even the United States, has suggested that such a merger statute impermissibly burdens interstate commerce, even though it quite obviously potentially stops the interstate, international commerce of control.

Even though the United States concedes the fundamental premises on which the CTS argument rests, it nonetheless argues that the statute is unconstitutional under the commerce clause because its provisions on voting rights are triggered by purchase and sale, what they call transactions involving shares, and although there is no facial discrimination between interstate and intrastate commerce, most of these transactions as they are called would take place in interstate commerce and the statute preserves whatever pattern of voting rights exists at a given time against transactions that would alter that pattern in significant ways.

But each of the United States' points is refuted either by decisions of this Court, or its own argument. That there can be transactions at all is purely a function of state law. This Court squarely held that in Aldridge.

Transferability of shares in a corporation stems from state law. Characterizing the triggering event for application of the statute as a "transaction" adds nothing to the analysis.

The easiest way to demonstrate that for the Court's purposes is to take a look at the partnership laws. Again, partnerships are creatures of states. State laws inherently say, virtually without exception, you cannot transfer the voting power inherent in a unit of a limited partnership or inherent in a general partnership interest without the agreement of somebody else, either the general partners or the limited partners as the case may be.

If this statute falls on that basis, likewise every partnership law has to fall on the same basis because those are transactions where the economic benefits are transferred and the voting rights are, to use the term so often used by the other side and by the Court, stripped by virtue of the transaction.

To bring it home, one of the hottest products hitting the intrastate market today is units in master limited partnerships. No one can seriously contend that state partnership laws violate the commerce clause because the voting rights are stripped away, even though that's plainly an interstate commerce kind of transaction.

The United States argument says that most transactions occur in interstate commerce, but that likewise adds little to the analysis. This Court has totally refuted a disproportionate impact theory in its decision in Exxon and in its decision in Commonwealth Edison Co. versus Montana in which this Court upheld direct burdens which fell disproportionately on interstate commerce.

Morever, if there is an impermissible disproportionate impact arising from the control share acquisition statute, that must be equally true of merger statutes because in mergers, no less than in controlled transactions, the shareholders have the right to accept or reject something that the state says is significantly and sufficiently important that they have the right to vote. The great bulk of merger transactions, no less than these kinds of transactions, will occur in interstate commerce.

The United States has apparently recognized this particular weakness in its argument, and attempts to distinguish mergers because they involve structural changes. But I have found no evidence in decisions of this Court or in the Constitution itself that says that there is any difference between structural changes, fundamental changes, transactional changes or anything else. It simply does not arise out of the commerce clause.

Moreover, merger are often accomplished in a way that --

QUESTION: That was a little too quick, there. There is some balancing involved in commerce clause cases, and arguably a structural change alters the balance more than some other kinds of changes. A state may have more of an interest in preventing a structural change than in preventing an ownership change.

MR. STRAIN: Justice Scalia, you raise, really for me to issues. Balancing is certainly language that this Court has used often, but it is possible to look at virtually every one of those cases, and there is only one exception cited by the United States, as either a discrimination case or a multiple burden, multiple and inconsistent burden case, and we set that out in the brief.

Let me take it another way for you. The state defines "structure." That is the starting point, so it's not a question of balancing at all. It's a question of what property rights does the state give, and that's for the state to define.

If it is to be otherwise, then there is a way to handle the problem and that is to go to the United States Congress where these kinds of issues are supposed to be, and have the United States Congress define for us what the interstate market in corporate control is. But historically, that hasn't happened. It certainly hasn't happened to date.

Have I responded to your question adequately? We'll find out, won't we.

What is key from our standpoint is whether the chartering state is allowed to say, or allowed to believe that certain changes in the entity owned by the shareholders are so important that the shareholder should have a voice in whether those changes occur. Whether a change is called structural, transactional or anything else has little to do, if anything, with the shareholder's ultimate interest.

Again, to bring that home, a shareholder is as cut out from the process of controlling his investment that if a single dominant shareholder elects the board of directors as he is if he receives a nonvoting preferred stock in exchange for his common stock in a merger transaction. The effect on him is precisely the same.

CHIEF JUSTICE REHNQUIST: Thank you, Mr. Strain. We will resume there at 1:00 o'clock.

AFTERNOON SESSION

(1:00 p.m.)

CHIEF JUSTICE REHNQUIST: We will hear from you now, Mr. Pritchard.

ORAL ARGUMENT OF JOHN F. PRITCHARD
ON BEHALF OF APPELLANT DYNAMICS CORPORATION
OF AMERICA, ET AL.

MR. PRITCHARD: Mr. Chief Justice, and may it please the Court:

QUESTION: May I ask at the outset -- I don't know why whenever I speak somebody looks over there -- what is the status of this controversy now? Has the takeover been accomplished?

MR. PRITCHARD: The shares have been purchased. The statute was held to be unconstitutional, Your Honor, and for that reason the vote that the statute provides for has not been held.

QUESTION: So, no question of mootness?

MR. PRITCHARD: No. No, Your Honor.

With the Court's permission I would like to direct myself to the practical impact of the Indiana statute, because it was Judge Posner's findings on this score that led him to strike the statute on commerce clause grounds. He concluded, we believe improperly, that the statute failed the tests set out in Pike v.

Bruce Church because the benefits that it imposed on interstate commerce were excessive in relation to its putative local benefits.

It is worth noting at the outset that the record contains no evidence whatsoever concerning either the burdens or the benefits of the statute, nor has there been any experience under this statute or under any similar statute which might shed any light on the subject.

Accordingly, the findings of the court below were based solely on speculation and this Court is not required to pay them any special deference. Now, addressing the burden side --

QUESTION: You deny that the statute would have the effect that Judge Posner speculated it would?

MR. PRITCHARD: Yes, Your Honor.

QUESTION: You don't think it would have any effect on takeovers?

MR. PRITCHARD: We believe that takeovers would be able to occur on essentially the same time schedule and using essentially the same procedures that they occur on now. The only difference --

QUESTION: Where they occur?

MR. PRITCHARD: Excuse me, Your Honor?

QUESTION: Where they occur.

MR. PRITCHARD: Where they occur -- tender offers do not always succeed, Your Honor. They would not always succeed under the Indiana statute. But we don't believe, for reasons I will get to, that the Indiana statute imposes any significant burden on the conduct of these corporate wars.

We are really talking about hostile tender offers, not friendly offers, in the context of the Indiana statute.

QUESTION: I would be interested to hear.

MR. PRITCHARD: Judge Posner concluded in his opinion that the statute, in his words, set up a gauntlet that few tender offers could run. This is strong and colorful language, but on what basis did he reach these conclusions?

He gives us only two reasons. First, since in his view no rational bidder seeking control of an Indiana corporation would purchase the shares without knowing the outcome of the shareholder vote, and since the shareholder vote could not transpire except after 50 days, that the statute as a practical matter imposes a 50-day delay on the consummation of tender offers and he considered that this would be burdensome.

Second, he stated that by virtue of the fact that the statute requires a shareholder vote, the success of the offer is, as he put it, subject to the tender mercies of the existing shareholders of the company.

On the first point, we submit that Judge Posner was simply wrong because he failed to consider the practical alternatives that are open to a bidder in a tender offer to which the statute applies. We demonstrate in our brief that nothing in the statute delays the commencement of a tender offer.

There is no pre-notification requirement like the one that this Court dealt with in MITE. Nothing in the statute prevents shareholders from tendering their shares immediately to the bidder, to the bidder's escrow agent, as soon as the offer has been made.

And importantly, nothing in the statute prevents the bidder from accepting the shares that have been tendered for payment, thus consummating the purchase immediately after the minimum 28-day waiting period that is provided for in the SEC's rules.

We may concede Judge Posner's point that many bidders seeking control would want the voting rights issuie resolved before they paid for the stock. But this desire is easily accommodated as the bidder could request the shareholder election on the same day he presents the offer, and structure the offer so that the acceptance of the tendered shares for payment was conditioned upon the later outcome of a favorable vote on the voting rights issue.

This would have the effect of locking up the stock so far as the bidder was concerned, and it would also cut off shareholders' right to withdraw their shares after the acceptance.

Your Honors, this procedure is not new. It is followed every day in many tender offers which are subject to conditions such as the receipt of required regulatory approvals such as those imposed by the Federal Communications Commission, by the Federal Reserve Board, by the Insurance Commissioners of various states who are required to approve a transfer of control before it takes place.

It is also followed when offers are conditioned on the dismantling of certain defenses that the targets of these tender offers have erected, such as poison pills, so that to condition the acceptance for payment on the receipt of voting rights is no different from the practice that prevails in other contexts routinely in the tender offer area.

In fact, so common is this practice that the SEC has provided explicit guidance on the subject in its interpretive releases which we quote in our brief. And it is instructive, we believe, that despite the opportunity to do so in its brief, the SEC did not take the position that the 50-day period for the election would result in any actual delay.

Even if the statute did delay the consummation of the purchase for 50 days, that period is limited. It is not an unlimited period as the Court dealt with in MITE. And I know it is only 22 days longer than the minimum period of 28 days that is prescribed by the SEC's own rules.

So, much more is required, we submit, than unsupported speculation to find that this so burdens tender offers as to render the Indiana statute unconstitutional. This is especially true, Your Honors, when there has been no showing that there are defenses which the target could put into place in 50 days that the target couldn't also put into place in 28 days.

Furthermore, we believe that no showing could be made that hostile tender offers can normallly be concluded in 28 days, given the litigation that swirls around these corporate wars.

Turning to the second point, Judge Posner felt that the shareholder vote, the fact that a shareholder vote had to take place, was a burden on interstate commerce. However, it seems self-evident that if the majority of the shareholders wished to tender their shares in response to a tender offer, they will also vote to confer voting rights because only by conferring voting rights will they be able ultimately to receive payment from the bidder.

QUESTION: His votes are excluded.

MR. PRITCHARD: No, Your Honor. The votes -- well, the bidder's votes are excluded but the votes of the shareholders -- excuse me.

QUESTION: He is trying to get another 11 percent -- suddenly instead of needing just an 11 percent vote of the entire corporation he needs 50 percent of 60 percent, right?

MR. PRITCHARD: I am sorry, Your Honor. He only needs a majority of the disinterested shares. That would be the majority of the shares other than his own, so that he wouldn't need a super-majority, so to speak, of the shares of the entire corporation.

QUESTION: More than 11 percent, he would need 30 percent.

MR. PRITCHARD: Well, he would need 30 percent. That's right.

QUESTION: But that's 30 percent --

MR. PRITCHARD: But that's 30 percent of the disinterested shareholders.

QUESTION: It's 50 percent of the disinterested.

MR. PRITCHARD: Right, Your Honor, it is 50 percent of the disinterested.

QUESTION: But it's 70. If you counted his 40, it's 70 percent of the entire ownership of the company.

MR. PRITCHARD: But his 40 percent does not vote, Your Honor.

QUESTION: I understand.

MR. PRITCHARD: So that you are having --

QUESTION: By virtue of the statute.

MR. PRITCHARD: By virtue of the statute.

QUESTION: So, it's pretty much tantamount to a super-majority.

MR. PRITCHARD: It is a majority of the very shareholders who are interested in the outcome of the election and in tendering their shares. That is my point, Your Honor, and if a majority of the persons to whom the offer is directed wish to accept it because the price is so attractive, or for other reasons, they are entitled to do so.

QUESTION: Of the persons to whom it is directed, to get control, all he needs is 11 percent of the whole company, and you are now converting that into, he has to get 50 percent of all of the remaining shares in order to get --

MR. PRITCHARD: Your Honor, that is another question. The question, at what level a dominant shareholder actually acquires working control of a corporation is another matter.

We submit that at 33 and a third percent in publicly traded corporations, the dominant shareholder has working control. He has working control at 40. He has absolute control at 50.

CHIEF JUSTICE REHNQUIST: Thank you, Mr. Pritchard.

We will hear argument from you now, Mr. Sachnoff.

ORAL ARGUMENT OF LOWELL E. SACHNOFF

ON BEHALF OF DYNAMICS CORPORATION OF AMERICA, ET AL.

MR. SACHNOFF: Mr. Chief Justice, and may it please the Court:

Let me see if I can clarify Justice Scalia's and Justice Stevens' concern over the mathematics here, because it is important. Let's take this case.

Bidder, my client, owned approximately 27 percent. To may it easier, if the bidder had owned 20 percent and if the insiders who also have interested shares and were disqualified from voting, if they owned another ten percent that's 70 percent -- that's 30 percent which leaves 70 percent.

The statute requires a majority of the disinterested shares outstanding, but in all these cases -- in no case do all the shareholders vote. The average is about, let's say, ten percent. Now we are down to 60 percent

The statute also has a strange quirk because it doesn't disqualify the shares of directors who are not officers of the corporation, but we know because of structural bias who it is who puts those directors in. It's management, and those folks are going to vote for management for sure, not to give the vote to a prospective bidder here.

QUESTION: Mr. Sachnoff, when you said ten percent about the number of shareholders, did you mean ten percent don't vote?

MR. SACHNOFF: That is correct, Your Honor. That is correct, ten percent generally -- that's an oversimplification but for purposes of this hypothetical you never get all the shareholders of a public corporation to vote.

So, if you take it -- we are down, now, Justice Scalia, to 50 percent and the bidder has to get 36 percent of that 50 percent which is over 70 percent, as Justice Stevens figured out. That is one of the numerous things that takes this level playing field and begins to tilt it against the bidder.

I think that's a good introduction to the place I think this case ought to start and that is with Judge Posner's comments in his opinion, his lingering doubts about whether or not the Williams Act really pre-empts state takeover statutes such as this. And to put it in terms that this Court has stated on numerous occasions, the question is whether or not the state regulation or statute stands as an obstacle to accomplishing the purposes and the objectives of the Williams Act.

Now, if we remove these lingering doubts, and if Your Honors in this case do that, then it becomes unnecessary to get into the great silences of the commerce clause and it becomes unnecessary to go into the second branch that's troubled the lower courts in all of these cases, which is trying to figure out whether this is a strict scrutiny kind of case or whether it's a pike-balancing test case.

The focus out to be, at least, first on the Williams Act because I believe that Justice White's opinion, the plurality opinion, was quite correct. I think "crystal clear" is what he said. And that is that the Williams Act's principal purpose is to protect the shareholder, to protect the autonomy of the investor, and that autonomy is protected by maintaining this neutrality between the bidder on the one hand and management on the other.

That is the way that the shareholder's interest is protected. Now, the Indiana chapter and the other controlled share chapters like it in other states, tilt that balance drastically against the bidder and they do it in at least four or five different ways.

First off, they introduced this element of delay, and there is at least a 22-day delay and probably more because election contests generally occur in connection with what we are talking about, which is a proxy contest superimposed on a tender offer. A point that Mr. Strain and Mr. Pritchard didn't make is that every tender offer, every tender offer for an Indiana corporaton necessarily involves a proxy contest. That is, unless management says, okay, you can take over my company.

But that doesn't happen, as in this case. What happens is that the bidder has to have a proxy contest with management to try to get these votes, the 50 percent or the majority of the disinterested shares, and that proxy contest is an immense additional burden on the tender offeror which the Williams Act never contemplated.

Under the Williams Act a tender offeror makes a tender, sends out the solicitations to all the shareholders, and the shareholder in Oregon gets this letter in the mail that says, I'd like to buy your shares at this premium, and all the shareholder has to do is say yes or no.

In this case we need a proxy contest on top of that. Next, in addition to the delay, there is the uncertainty because a tender offer involves a tremendous amount of sunk costs. The sunk costs include all of the legal expenses and accounting expenses and printing and mailing.

In addition to that, in order to line up a tender offer that makes any sense at all, you have to be able to say to the shareholders of the corporation, we have the financing lined up to be able to make this tender offer. That financing involves commitment fees with merchant bankers and investment bankers usually in the range of one to one and a half percent, and on a $100 million tender offer, which is not a large one, that's a million and a half dollars.

So, we are talking about a tender offeror committing to spend two to three million dollars up front which he'll never get back at all if, as Judge Posner put it, the tender mercies of these outside shareholders, the disinterested shareholders, don't give that tender offeror the vote.

The statute is truly a gauntlet through which the bidder has to run in order to get the vote, in order to accomplish his or her principal goal in making a tender offer, which is getting control. The deck is stacked against the bidder and it's stacked against the bidder because of the vote that I discussed earlier. It's also stacked against the bidder because it takes away investor autonomy.

The purpose of the Williams Act is to provide information to the investor, to the shareholder, so that he or she can make an independent judgment, shall I tender my shares or not. And Justice O'Connor asked a question earlier, this is a strange way to protect shreholders' votes.

You say to the 20 percent shareholder, your votes are stripped away unless you go through all these hoops in order to get a majority of the disinterested vote, and what it says to the shareholder who is in Oregon who would like to tender his or her shares to the bidder in Connecticut or Florida is, you can't do it. You can't tender your shares unless the bidder runs this gauntlet and is able to get a majority of the supposedly disinterested shareholders to vote.

So, the process, looked at in a very practical way that Indiana imposes on the bidder, is a stacked deck. Just last night -- every time I read the statute I come up with something else, another little hoop to go through.

I really discovered this one. It's not in our briefs but it's in the statute. The statute provides for record date of 70 days before the meeting. That's in another section. It's in 2330.

The Controlled Share Act requires a meeting if requested by an acquiring person, within 50 days but that is 50 days. If the management sets a record date 20 days earlier, that means that there are 20 days of trading during which shareholders of that corporation will have sold their stock but still be record date shareholders for purposes of voting on whether or not this tender offeror has the right to vote these shares.

Those shareholders are going to get this proxy thing in the mail and they couldn't give two hoots whether or not the bidder gets the vote or doesn't get the vote because they are out of the corporation. And it's like a little archeological dig to go through that chapter but it is filled, as I said, with these pitfalls which tend to keep inclining that balance that Congress in the Williams Act said ought to be neutral, ought to establish this neutrality, keeps sloping it against he bidder.

What it adds up to is that it chills tender offers and deters them because it is true that no rational tender offeror is going to run this gauntlet, incur these expenses, and risk all this uncertainty where there is no guarantee, and in a process that is totally controlled by management when there is no guarantee that at the end of the line he is going to have the one thing he is looking for which is this vote, the vote which exists in the national market for corporate control.

QUESTION: Mr. Sachnoff, if you use the term "chill" to mean in any way discourage, as some of our cases have used that term, any added state requirement to federal requirements will "chill," in a sense. It's always harder to complete an additional requirement.

Your argument is something more here, I take it.

MR. SACHNOFF: Yes, it is, Mr. Chief Justice. It is a lot more, and perhaps in order not to overstate my case I shouldn't -- I can use the word "deter" because I lived with this tender offer in particular and my client would no more make that tender offer and put up the money that was necessary to purchase the shares unless there was certainty that the Indiana statute was declared unconstitutional for one reason or the other.

What I am really saying is that no tender offeror will take all of these chances to make a tender offer when this kind of a mine field is in front of him or her. It just won't be done.

Now, let me back off that for a minute. Chilling means interfering or deterring. You are adding additional burdens and I'm not sure that it's always impossible for a tender offeror to say, well, I'm going to take all these chances and make these tender offers anyway.

That's not -- that really isn't the say I read the legislative history of the Williams Act. I read it as meaning that Congress said that there is to be this neutrality in order to accomplish the goal that none of us disagrees about. We all agree that the principal goal is to protect shareholders and to protect investors.

There is a disagreement about whether or not that neutrality -- I think both Justice Stevens and Justice Powell raised this in the MITE case -- the question is whether that neutrality is an eternal neutrality to the Williams Act or whether it's something that's projected out onto the states.

I don't think we have to get into that thicket because I think it's clear that when you focus on protection of the investor -- this is Justice O'Connor's point -- the investor's autonomy is taken away by the Indiana statute.

The investor may not tender his or her shares without all these other things happening, and shareholders -- not even a control shareholder; a shareholder who only acquires 20 percent, 20.5 percent of the corporatin and, as we learned in this bidder proxy fight here, we had 27 percent, my client, we lost the proxy fight by a very slim margin.

Every day in the Wall Street Journal we read about proxy fights for public companies in which shareholders with major stakes in the company lose them. Judge Posner's view is that only 50 percent guarantees control.

We can debate that. I think 49 percent probably guarantees control. But certainly in the theoretical sense, 50 percent is needed.

So, my point is that it's not necessary to get to the commerce clause, the intricacies of the commerce clause in order to affirm the Seventh Circuit here and to make it unnecessary for the courts and litigants to do battle in the constitutional vineyards.

QUESTION: Of course, we may not agree with you on the Williams Act analysis.

MR. SACHNOFF: You may not.

QUESTION: Do you plan to address the commerce clause?

MR. SACHNOFF: I certainly do. On the commerce clause point, the unifying principle that I see in the commerce case is a look first at the local interests, the legitimacy of the local interest that is to be protected, and then whether it's the strict kind of scrutiny test under Hughes or under Lewis or whether it's the balancing test under Pike. You have to look at the burden and the extent of the burden on interstate commerce.

In the --

QUESTION: May I ask --

MR. SACHNOFF: Surely.

QUESTION: -- what the implications are of the Seventh Circuit's holding on the internal affairs doctrine, and does that holding mean that the courts are going to be faced with commerce clause challenges to a whole range of provisions such as cumulative voting and staggered boards and partnership voting and non-voting shares and all of that, because the whole panoply of corporation law and these restrictions that we find in state law can be said to affect the market for corporate control someway and that is sort of the theory of the Seventh Circuit.

MR. SACHNOFF: I think, Justice O'Connor, you are asking about the limiting principle, where does all this stop, and is it really true as appellants say that an affirmance here, a merger, a dissolution, sale of all the assets, staggered boards, things like that, is that those are either transactions directly involving the corporation of a very profoundly fundamental nature.

If you merge, a corporation can be merged out of existence. If a corporation is dissolved, of course that requires shareholder vote. And if a corporation is dissolved that requires shareholder vote also.

If a corporation is going to sell substantially all of its assets, that requires the shareholder vote too. Staggered boards and cumulative voting of course are going to have some sort of an impact on the interstate market for corporate control.

But the issue is, is the state operating within its traditional sphere of corporate governance activity involving the corporate transaction -- and all of the transactions Mr. Strain and Mr. Pritchard and I think Your Honor have --

QUESTION: Suppose the state just passed a law that said that acquisition of more than a certain percentage of shares is going to require the voting of all the stockholders, period.

MR. SACHNOFF: If that happened midstream and that was where I part company with the government in this case, if that happened in midstream, let's say that Indiana passed a statute that says no one can own and vote more than five percent of the stock of a corporation, that would make it almost impossible for that corporation to be taken over by any other corporation.

That kind of statutory provision would fail under the commerce clause analysis, and I believe under the Williams Act.

QUESTION: No, a statute that just says, before there can be an acquisition by an outsider of more than "X" percentage of the shares we are going to require all the other shareholders in the corporation to vote.

MR. SACHNOFF: That's this statute. In effect--

QUESTION: Well, this has a lot of other things.

MR. SACHNOFF: Part of the statute is that you don't get the vote, the bidder doesn't get the vote, without the vote of these so-called disinterested shareholders. I am taking that one step further because it is the principle advanced by Indiana that I think has no limitation and it has no stop.

They say that anything that affects the voting rights is something which is permissible in the state's sphere of regulation, so that I guess they come here with a straight face and say that if Indiana --

QUESTION: Yes, but what about the question I posed?

MR. SACHNOFF: What I am saying is that that's this statute, Justice O'Connor, and I believe that this statute fails both under the Williams Act and under the commerce clause because it is an obstacle to the accomplishment of the purpose of the Williams Act and because it does unduly burden interstate commerce.

I was trying to make the point with a hypothetical which takes it a little further and that is, if Indiana had said you have to have 90 percent, a 90 percent vote, there's a point out there at which these fundamental corporate matters that Your Honor is addressing now would become impediments, would become obstacles under the Williams Act and burdens under interstate commerce.

QUESTION: Yes, but in a sense some of these obstacles actually can be said to enhance the ability of the shareholder to protect himself or herself. The fact that the shareholder is permitted to act in a group situation with the benefit of disclosure of all that's going on, can actually enhance the stockholder's opportunity to maximize a return on the shares.

MR. SACHNOFF: I think that may be true but I think that that's got to be a political decision in the interstate market for corporate control that ought to be done by Congress and not by individual states.

QUESTION: Isn't that exactly the kind of thing that's a legitimate thing for a state to be concerned about, if the corporation is incorporated in that state?

MR. SACHNOFF: Your Honor, I think that would be true if this were the 51st state that were incorporated behind some John Rolls veil of ignorance and there were no shares outstanding, I think that analysis would be absolutely correct.

But what we are saying is that in midstream -- Indiana of course has launched all these shares. They are all out there trading in interstate commerce right now, and if in midstream Indiana or any other state says, we're changing the rules and we're going to prohibit a transfer of shares in effect from one shareholder to another, I believe that under those circumstances it runs afoul of both the Williams Act and the commerce clause.

There is a difference between starting on a clean slate and interfering with commerce in both the shares and in corporate control that already exist, because that commerce --

QUESTION: Are you saying the statute is perfectly all right, then, for corporations which are organized after the passage of the statute?

MR. SACHNOFF: If a state wanted to do something as foolish as to have two different kinds of voting requirements -- that is grandfather clause -- I think it probably would be. It probably would be because in that sense there would be no frustration of any expectation of people who trade in the market for corporate control or for corporate shares.

So, I think if a state wanted to make that distinction it would be okay. It's imposing it in the middle upon shares that are already being traded in interstate commerce.

QUESTION: Doesn't the -- the target corporation is the one that chooses to be governed by it, isn't that --

MR. SACHNOFF: The target corporation starts out, of course, Justice White, governed by the particular laws of the chartering state. I guess --

QUESTION: But could it decide not to, didn't want to have to comply with these provisions?

MR. SACHNOFF: It's a book-of-the-month, sort of, it's a negative enrollment scheme in Indiana. All the corporations are covered in August of -- in this month unless you opt out, which of course is one of the problems of that statute because that is the one that permits the discrimination in favor of Indiana corporations.

It's a little bit like the Court's decision in the Raymond case on truck lengths, where one of the reasons the statute was struck down was because the regulatory scheme permitted the regulators to discriminate in favor of the Wisconsin trucks. But you are right, Justice White, and that is that the corporations can opt out which is again one of the problems with the statute that causes it to be discriminatory at the option of management in favor of the Indiana corporations. That is correct.

QUESTION: I don't understand that. Say that again.

MR. SACHNOFF: I might lose you, Justice.

QUESTION: Since nobody else is subject to it anyway except Indiana corporations, how can the opting out provision lean in favor of Indiana corporations only?

MR. SACHNOFF: Because if the management of an Indiana corporation is faced with a friendly -- management opts in the statute, it doesn't opt out after August of '87, so they are within the statute and they are opposing a prospective takeover by a Connecticut corporation or a New York corporation, and what they do then is they arrange to have a friendly takeover with an Indiana corporation and then they can simply opt out of the statute.

That is, opting out means that Indiana corporation or any corporation it favors can acquire the vote without having to have --

QUESTION: But not just an Indiana corporation. I mean, they can --

MR. SACHNOFF: Or any friendly corporation.

QUESTION: Any friendly corporation. So, it would be discrimination but not discrimination that has anything to do with the commerce clause.

MR. SACHNOFF: That's true. What it does is --

QUESTION: It's not only true. It's the only point that's relevant, isn't it?

MR. SACHNOFF: But it puts in management's hands, Justice Scalia, the option to be able to say, I favor this prospective bidder over the other one, which is not the purpose of the Williams Act and the tender offer.

QUESTION: Different point.

MR. SACHNOFF: Different point. That's on the commerce clause.

Another point that I wanted to make is that Mr. Strain in the beginning of his presentation indicated that perhaps there was a misstatement in CTS's reply brief, and it is an important one because the government has filed a brief in this case, two branches of the government, the government -- that is, the Justice Department and the Securities and Exchange Commission.

Both the Justice Department and the Securities and Exchange Commission support DCA, our position, and that is that the commerce clause renders the Indiana statute invalid because of the excessive burdens. But in the reply brief CTS says in effect that the SEC also throws in the towel on the Williams Act; that is, that the SEC says that the Williams Act does not pre-empt the field.

It is an important point, that that is not the case; that the government's brief is very carefully drafted in such a way that it is only the Justice Department and not the SEC that says the Williams Act doesn't pre-empt the statute, because of course the SEC argued in MITE, the SEC argued in Kidwell, the SEC argued in Household in the Delaware Supreme Court that the Williams Act did in fact pre-empt those state statutes because it was an obstacle to tender offers, got in -- as they say, got in the way.

The other point that I wanted to make, which is also raised in the reply brief that was filed by CTS and we didn't have, obviously, a chance to respond in writing, is this notion that this is only a private matter, private individuals, and the state really isn't involved in the obstacles to the Williams Act or the burden on interstate commerce.

That point is sort of stunning because Indiana has enacted a blueprint, a very detailed blueprint here, under which the corporations chartered by the State of Indiana can invoke these burdens and obstacles and it's subject to the same kind of analysis that this Court has done on many occasions under the Fourteenth Amendment because finding state action means finding a state that provides an impetus or a blueprint for private individuals to violate rights.

Obviously, only states can violate the

commerce clause in the same sense that individuals generally have their rights that are violated under the Fourteenth Amendment. So that, this blueprint is such a complete and detailed prescription for management of target corporations that it is very clear that the State is behind this.

QUESTION: What if the State changes its corporate law to say that shares are not transferable at all? Would that violate the commerce clause?

MR. SACHNOFF: Yes, it would, Justice Scalia. It would violate the commerce clause if it said shares are not transferable and those shares have already come to rest in the hands of all of the shareholders in the country. It would violate the commerce clause because it would be -- it would place a burden on interstate commerce that had no relationship I can think of, as I stand here now, to a legitimate corporate concern of the state.

I don't -- maybe you can help me, but I can't think of any right now, to make shares not transferable. Corporations would --

QUESTION: But it would be okay in the future, it's just --

MR. SACHNOFF: It would be okay in the future. It would be okay if it didn't upset the present market for these goods and these items, yes, it would have to be in order for my analysis to be consistent and correct.

QUESTION: I really don't see the distinction you draw between present and future as far as the commerce clause is concerned. I can see a lot of difference as far as whether it's a taking by the state or something of that sort, but why should it make any difference as far as the commerce clause is concerned?

MR. SACHNOFF: It's because there is a present market. There is a present market in the country for the shares of a corporation that's chartered in Indiana.

QUESTION: You mean, if a state -- if New York enacts a law that says no Florida grapefruit can come into New York, it would be good if Florida grapefruit had previously been coming in or bad if they had previously been coming in but good if there had never been any Florida grapefruit before?

MR. SACHNOFF: I think that that's a different situation.

QUESTION: Well, I don't see why. It seems to me you can't for purposes of the commerce clause impede future commerce any more than you can present commerce, can you?

MR. SACHNOFF: Because, Your Honor, my example maybe works better with a new state rather than taking a state which changes the law prospectively, there is no commerce in the shares of the new state, the 51st state, and there is no commerce, I think in the shares of the new corporation in "X" state as to which there is no transferability or no vote.

So that, any corporation that is foolish enough to incorporate in a state that had that kind of restriction, you'd be unable to raise capital. The capital markets would walk away from a corporation like that in a flash.

If you take that state chartered corporation with those kinds of restrictions and do it willingly, then you subject yourself to those restrictions.

QUESTION: Well, Mr. Sachnoff, your argument strikes me as a little bit at odds with this Court's case in Exxon against Maryland where the state law was enacted and it clearly favored in-state retailers at the expense of out-of-state suppliers. Ninety-five percent of the suppliers were from out of state and the Court said that didn't make any difference.

MR. SACHNOFF: Your Honor, in Exxon -- I view Exxon as analogous to the blue sky laws because it had to do with products coming into Maryland and it had to do with the fact that the state regulation there didn't interfere with the ability of interstate suppliers to sell their wares in Maryland.

It only said that vertically integrated suppliers couldn't have retail outlets in Maryland but it didn't deprive Maryland of the opportunity to have a full range of petroleum products and at the same time -- I think it was Justice Stevens who said that the commerce clause doesn't require that interstate markets be totally efficient.

There was some inefficiency involved in that but it didn't stop -- it didn't stop the products from coming at all into Maryland. They came in, in a different way.

QUESTION: This statute may not totally stop; it may deter?

MR. SACHNOFF: I think, again from a practical point of view as I see the decisions in this Court on the commerce clause, the focus is on the practical impact of the statutes from a practical point of view. It stops the Connecticut bidder from buying a share from the Oregon shareholder in this market that really has next to nothing to do with the internal governance matters of a corporation.

My last point is to respond to Justice Powell's point about whether or not the statute is designed to protect state businesses and I think the State of Indiana's brief indicates that it is designed to check the removal of Indiana corporations. And my point there is that there are lots more less intrusive ways of doing that than interfering with interstate commerce or setting up an obstacle to tender offers under the Williams Act.

The states have senators who can lobby in the national Congress. States really ought to, if they want to attract and keep business, they can set up Silicon Valleys and Route Ones. They can provide tax subsidies for industries. But that's the kind of competition I think the commerce clause was designed to stimulate among the states.

Lastly, the ingenuity of corporate takeover lawyers apparently known no bounds. They come up with the evolution of poison pills which have been upheld by the courts as a means of blocking or thwarting unwanted takeovers.

So, there are presently in place structures that can accomplish the goal, the concern that I believe Justice Powell raised both in the MITE case and here today.

If there are no other questions?

CHIEF JUSTICE REHNQUIST: Thank you, Mr.

Sachnoff.

The case is submitted.

(Whereupon, at 1:38 o'clock p.m., the case in the above-entitled matter was submitted.)

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lderson Reporting Company, Inc., hereby certifies that the ttached pages represents an accurate transcription of lectronic sound recording of the oral argument before the upreme Court of The United States in the Matter of:

#86-71 - CTS CORPROATION, Appellant V. DYNAMICS CORPORATION OF AMERICA, E AL.; and

#86-97 - INDIANA, Appellant V. DYNAMICS CORPORATI_N OF AMERICA, ET AL.

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