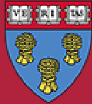
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The Long-Term Value of the Poison Pill

Posted by Martin Lipton, Wachtell, Lipton, Rosen & Katz, on Friday, December 18, 2015

Editor's note: Martin Lipton is a founding partner of Wachtell, Lipton, Rosen & Katz, specializing in mergers and acquisitions and matters affecting corporate policy and strategy. This post is based on a Wachtell Lipton memorandum by Mr. Lipton, Daniel A. Neff, David A. Katz, Mark Gordon, and William Savitt. This post is part of the Delaware law series; links to other posts in the series are available here. Related research from the Program on Corporate Governance about poison pills includes Toward a Constitutional Review of the Poison Pill by Lucian Bebchuk and Robert J. Jackson, Jr. (discussed on the Forum here), and The Case Against Board Veto in Corporate Takeovers by Lucian Bebchuk.

Nearly six years ago, Air Products made an unsolicited all-cash bid to acquire Airgas for $60 per share (later increased to $70), to which the board of directors of Airgas said "no." Based on the Airgas directors' unanimous judgment—informed by months of thoughtful review and analysis—that Airgas was worth more than Air Products was offering, whether on a standalone basis or in the hands of another industry player, this "no" was made possible by bedrock principles of Delaware law. These principles recognize that it is the role of the board, and not raiders or short-term speculators, to determine whether and when a company should be sold, and authorize the use of appropriate measures—most notably, the poison pill—to ensure the board has the opportunity to perform this essential function.

Last month, in vindication of the Airgas board's judgment and confirmation of the wisdom of the Delaware case law (particularly the Delaware Chancery Court's 2011 *Airgas* opinion validating the use of the poison pill), Airgas agreed to be sold to Air Liquide at a price of $143 per share, in cash, nearly 2.4x Air Products' original $60 offer and more than double the final $70 offer, in each case *before* considering the more than $9 per share of dividends received by Airgas shareholders in the intervening years.

The value created by the Airgas board can be seen in this table comparing the benefit of having held a single share of Airgas continuously from the time of Air Products' bid vs. the value of having accepted Air Products' bid and then reinvesting the proceeds in the S&P 500, in each case with all dividends reinvested. The results are shown on a total shareholder return ("TSR") and current value basis:

		Airgas Standalone, without Air Products Deal		Investor Receiving Air Products' Offer Price, with proceeds invested in the S&P 500
Measured from termination of final $70 bid (2/15/11)*	TSR	143%	*vs*	88%
	Current Value	$156	*vs*	$121
Measured from start of original $60 bid (2/5/10)**	TSR	264%	*vs*	205%
	Current Value	$158	*vs*	$133

Airgas' success reminded us of the long term success of McGraw-Hill, which rejected a high-premium, all-cash takeover bid in 1979 (See our memo Just Say No, December 5, 2014). In the 35 years following that rejection, McGraw-Hill's shareholders experienced TSR of 13,263% compared to approximately 5,280% for the S&P 500.

The Airgas and McGraw-Hill results provide clear rebuke to critics of the poison pill and to critics of board-primacy generally, who have argued that takeover defenses lead to board entrenchment and that boards do not possess the judgment and skill to know better than "the market" the long-term value of the corporation. To the contrary, in our experience, boards work very hard to do the right thing in takeover situations, carefully assessing industry and general economic conditions, their company's probability-weighted prospects and the associated risks and uncertainties, and the timing of—and possibility of opportunism in—the unsolicited bid.

While Airgas' and McGraw-Hill's respective successes from saying no (and other such successful examples) do not mean that saying no is always the right answer to every unsolicited takeover bid, it does show that the points we have been making since 1979 remain true today:(1) boards have proven remarkably adept and successful in exercising their discretion in the takeover context; (2) this success discredits those who claim their studies "prove" that board discretion in any individual situation leads to the wrong outcome for shareholders; and (3) because each context is different, it is wrong to adopt one-size-fits-all policies that restrict or undermine the ability of a board to "just say no" (or that attack a board merely for doing so) in a situation where the board, exercising its fiduciary duties, determines the bid is not in the best interest of the shareholders.

* TSR from February 16, 2011 (the date after the Chancery Court decision upholding Airgas' use of the poison pill) through November 18, 2015, with dividends reinvested, and assuming an initial investment of $64.35, the Airgas closing price on February 16, 2011. Current value assumes ownership from February 16, 2011 through November 18, 2015, with dividends reinvested. Current value of continuous Airgas investment is based on Air Liquide deal price of $143 per share. Offer proceeds assumed to be $70 per share, in cash.

** TSR from February 5, 2010 (the date of first public announcement of Air Products' all-cash $60 bid) through November 18, 2015, with dividends reinvested, and assuming an initial investment of $43.53, the Airgas closing price on February 4, 2010. Current value assumes ownership from February 5, 2010 through November 18, 2015, with dividends reinvested. Current value of continuous Airgas investment is based on Air Liquide deal price of $143 per share. Offer proceeds assumed to be $60 per share, in cash.