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Defensive Changes in Corporate Payout Policy: Share Repurchases and Special Dividends

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ABSTRACT

This paper examines defensive payouts announced in response to hostile corporate control activity. The evidence indicates that the announcement of defensive share repurchases is associated with an average negative impact on the share price of the target firm. In contrast, special dividend payments generally increase the wealth of target firm shareholders. Regardless of payout type, those firms remaining independent after the outcome of the corporate control contest experience an abnormal share price increase over the duration of the contest. Among these firms there are substantial post-contest changes in capital, asset, and ownership structure and abnormally high rates of top management turnover.

RECENTLY FINANCIAL ECONOMISTS HAVE explored the link between corporate financial policies and the market for corporate control. Jensen (1986a, b) argues that a major cause for takeover activity is the conflict between managers and investors over the payout of free cash flow. A leverage-increasing takeover or restructuring can increase firm value since it commits managers to pay out free cash flow rather than invest in unprofitable projects. Harris and Raviv (1988) and Stulz (1988) modeled changes in capital structure and how they can be used to alter voting rights within the firm, in some cases effectively deterring hostile takeover attempts. Dann and DeAngelo (1988) empirically examined a broad class of defensive adjustments in asset and ownership structure and concluded that the primary motivation for these transactions appeared to be the entrenchment of the target firm's management team.

This paper investigates a specific type of defensive adjustment in financial policy that has become increasingly popular in recent years: the use of special payouts to shareholders through share repurchases or special dividends. In share repurchases, managers may choose not to sell their shares in the repurchase offer. Similarly, in the special dividend plans studied here, managers typically receive additional shares instead of cash. Hence, both types of payouts can result in the concentration of voting power in the hands of managers. As emphasized in Stulz (1988), this may lead to either an improved incentive structure within the firm or the entrenchment of the current management team. The magnitude and impact of such changes resulting from defensive payouts is thus an interesting empirical question.

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The results presented here indicate that these alterations in payout policy contribute to an overall defensive strategy through which a high percentage of target firms maintain their independence. They lead to large changes in both the capital structure and the structure of voting rights within the firm. Evidence on the wealth effects of these transactions suggests that while both types of payouts are associated with increases in the value of the target firm relative to its pre-takeover contest value, share repurchases are generally inferior alternatives to those presented by hostile bidders. The announcement of a defensive repurchase is associated with a significant decrease in the wealth of target firm shareholders. Furthermore, the withdrawal of a hostile bidder subsequent to a defensive repurchase announcement results in large losses for target firm shareholders. In contrast, special dividend announcements typically increase the wealth of target shareholders.

An examination of those firms remaining independent after announcing a defensive payout suggests that there are substantial structural changes in these firms after the outcome of the control contest. In addition to large changes in both the capital and ownership structures of the firm, there is an abnormally high rate of top management turnover in the three years following the outcome of the control contest. Furthermore, the target firms frequently embark upon restructuring programs that are directly tied to the previous hostile control activity and to the defensive payout. This evidence suggests that the market for corporate control serves as an effective disciplinary force even in those cases where managers are able to successfully deter a hostile bidder.

Section I presents the sample selection procedure and descriptive statistics for the sample of forty-nine defensive payouts. In Section II the impact of these transactions on the wealth of the firm's shareholders is examined. Section III presents evidence on the extent of influence that defensive payouts had on contest outcomes. Section IV provides evidence of major structural changes in those target firms that retain their independence, and Section V concludes.

I. Defensive Share Repurchases and Special Dividends

A. Sample Selection

The sample selection procedure attempts to isolate those cases in which there has been some disbursement of corporate resources to shareholders during the course of a corporate control contest or in response to the threat of a change in control. These transactions are identified by examining the *Wall Street Journal Index* listings of those firms mentioned in the *Wall Street Journal Index* under the headings "Mergers and Acquisitions" or "Reacquired Shares" during the period 1980–1987. A transaction is included in my sample if it involved a general repurchase of shares or some special payout to shareholders subsequent to an actual takeover bid or the threat of some change in control.

These threats take many forms, including 13-d filings, published rumors of takeover bids, and discussions among management teams. For example, after Leucadia National Corp. acquired a 5.3% stake in GATX Corp., GATX "... announced a $152 million share repurchase that is part of an anti-takeover defense."

Table I

Profile of Sample Payouts

Profile of 49 defensive payout announcements over the sample period 1980–1987.

Panel A: Time Profile

Year	Number of Firms Announcing Defensive Payout Plans	Percentage of Total Sample
1980	1	2.04
1981	2	4.08
1982	2	4.08
1983	2	4.08
1984	2	4.08
1985	9	18.37
1986	19	38.78
1987	12	24.49
Total	49	100.00

Panel B: Profile by Payout Type

Payout Type	Number	Percentage of Total Sample
Open-Market Repurchases	10	20.41
Repurchase Tender Offers	16	32.65
Exchange Offers	7	14.29
Unknown Repurchase Type	7	14.29
Special Dividends	9	18.37
Total	49	100.00

(*Wall Street Journal* 5/16/86). Targeted repurchases (greenmail) are excluded from the sample.[1]

As noted in Dann and DeAngelo (1988), this type of sampling procedure most likely understates the incidence of these types of takeover defenses since those that are put in place prior to any rumored hostile activity are excluded from the sample. However, since my sampling includes those transactions associated with rumored hostile control changes, it permits the examination of cases where management erects a structural barrier which effectively preempts a takeover bid from the rumored hostile party. Also, to the extent that *Wall Street Journal* listings are biased towards larger firms, the sample may reflect this bias as well. (Appendix A lists the firms included in the sample as well as the announcement date of each defensive payout.)

Table I lists the sample by year of the payout announcement. A striking observation is the increasing use of share repurchases and special dividends in

[1] Greenmail payments are excluded since they do not represent general payouts to the target firm shareholders. However, there are similarities between greenmail transactions and the transactions studied here. Both represent a defensive action taken by target firm managers as a result of the possibility of a hostile control change. As will be shown in Tables III and IV, both also display average abnormal returns that differ from those typically associated with share repurchases. [See Dann (1981) and Vermaelen (1981) for evidence on general share repurchases and Bradley and Wakeman (1983) and Dann and DeAngelo (1983) for evidence on targeted repurchases.]

recent years. Over 80% of the sample observations occurred in the last three years of the sampling period, 1985–1987. The defensive payouts took many different forms. These include open market repurchases (10 cases), repurchase tender offers (16 cases), special dividend payments (9 cases), and exchange offers of debt securities and cash for shares (7 cases). In another seven cases it is not clear from financial press reports which form the payout would take. These firms merely announced their intention to repurchase some shares without specifying how the repurchase would be effected. For example, in response to a takeover proposal from Mesa Limited Partnership, "Diamond Shamrock Corp. is expected ... to buy back a significant portion of its shares." (*Wall Street Journal* 12/4/86).

The special dividends studied here differ from those not connected with a takeover contest [e.g. Brickley (1983)]. On the basis of *Wall Street Journal* reports, it is apparent that managers typically do not participate in the distribution, but receive additional shares instead. This is clearly the case in seven of the nine announced dividends. In the other two cases, management participation cannot be determined from the initial announcement.

There are two main types of special dividend plans used by the sample firms. In one type, shareholders received a cash dividend while managers received additional shares. In the other type shareholders exchanged each of their shares for cash and one share in the newly recapitalized firm. Managers exchanged each of their shares for additional new shares.[2] Thus in either type of distribution managers increased their fractional stake in the firm.

B. Characteristics of Target Firms and Defensive Payout Plans

Table II describes general characteristics of the firms that chose defensive payouts and of the payout plans themselves. Items (1)–(3) indicate that the target firms were generally quite large, older firms. Mean equity value and annual sales revenue were $1,741 million and $3,400 million, respectively. The typical target firm had been incorporated for about 54 years.

Items (4) and (5) describe the capital structure and structure of voting rights for the target firms. The average firm carried a moderate amount of long-term debt, approximately 21% of the total book value of its assets. As is true for the majority of large firms, managerial/board ownership of common stock was quite low. The beneficial ownership of officers and directors averaged only 5.2% with a median of 2.0%.[3]

Finally, item (6) measures the size of each announced payout relative to the pre-announcement value of the firm's equity. The data indicate that these

[2] An example of this type of distribution is the plan adopted by FMC. FMC proposed an exchange of $70 cash and one new share for each old share held by public shareholders. In contrast, instead of the cash dividend, management and the firm's PAYSOP received 5 ⅔ new shares for each old share.

[3] By way of comparison, Morck, Shleifer, and Vishny (1988) reported that in their sample of 456 of the Fortune 500 firms, the average board ownership was 10.6% (median = 3.4%). Similarly, Brickley, Lease, and Smith (1988) documented an average of 10.1% ownership by board/officers for a sample of 191 firms that proposed antitakeover amendments.

Table II

Attributes of Target Firms and Payout Plans

Mean and median values of selected attributes of target firms and defensive payout plans for the sample of 49 announced payouts over the period 1980–1987. The selected attributes are obtained from a number of sources. Item (1) is based on the closing price and number of shares reported in Standard and Poor's *Security Owners Stock Guide* approximately two months prior to initiation of the control contest. Items (2)–(4) are obtained from *Moody's Manual* for the year prior to the control contest. Item (5) is obtained from the last proxy statement before the control contest. Item (6) is calculated based on reports in the financial press and is esimated relative to the market value expressed in item (1).

	Mean	Median
Firm Size/Age		
1. Market value of common equity ($mill.)	1741	1065
2. Sales revenue ($mill.)	3400.3	1804.4
3. Corporate age at the time of payout announcement	53.6	55
Capital/Ownership Structure		
4. Long-term debt as a percentage of total assets	21.1	17.9
5. Percentage beneficial ownership of officers and directors	5.2	2.0
Payout Plan		
6. Size of defensive payout as a percentage of target firm's equity value	45.0	34.0

transactions were of significant size, averaging about 45% of the target's equity value.[4] The announcements frequently did not contain detailed information on the financing arrangements for the payout but what information there is suggests that they were primarily debt financed. Of the 19 transactions for which the *Wall Street Journal* contains financing information, 18 list debt as the primary financing source. Hence, although the announcements frequently did not include information on management participation in the proposed payouts, transactions of this size do have the potential to dramatically alter the capital and ownership structures of the firm. This issue is addressed in more detail in Section IV.

The characteristics of the sample firms were strikingly similar to those documented in Dann and DeAngelo's (1988) study of defensive restructurings despite the fact that there was very little overlap in the two samples. This observation lends additional support to Jensen's (1986a, b) conjectures regarding the types of firms that are the most likely candidates for restructurings. He argues that firms of the type in Table II are most susceptible to agency problems associated with free cash flow. A restructuring allows the firm to effectively bond itself against overinvesting free cash flow.

[4] These calculations are made based on the number of shares outstanding and the market price of these shares approximately two months prior to the initiation of the control contest. The fraction understates the true relative transaction size in those cases in which firms announced a recapitalization, and shareholders received a special dividend plus a share in the recapitalized firm. In these cases, only the dividend payment is used to compute the relative size of the transaction.

II. Defensive Payouts and Shareholder Wealth

A. Announcement Period Effects

The marginal impact of the payout announcement on the wealth of target firm shareholders can be ascertained by examining abnormal returns during the two-day period including the day before and the day of the payout announcement in the *Wall Street Journal*. Standard event study methods are used to compute returns in excess of those predicted by a market model regression.[5] Table III reports summary measures of the two-day announcement effects. For the full sample of 49 payouts, the evidence indicates that the typical announcement was associated with an increase in shareholder wealth. Over the two-day period, the target firm's share price experienced an average 1.88% abnormal increase in value.

A potentially confounding influence in assessing the marginal wealth effects is the presence of other information implicit in the payout announcement. By construction, the sample includes payout announcements coincident with the first public revelation of hostile control activity. For example, USG Corp. announced that it would ". . . buy back as much as 20% of its shares. The move is an apparent effort to fend off advances by the Belzberg family and make the company less attractive as a takeover target" (*Wall Street Journal* 11/21/86). Consequently, the announcement of the payout may have contained information about the probability of a takeover bid or other change in control.

To account for this possibility, Table III also reports two-day abnormal returns for the sample of 40 defensive payouts for which there had been some prior indication of corporate control activity.[6] The evidence indicates that the implicit information effect was quite important. For these announcements, announcement period abnormal returns averaged −0.83% ($Z = -2.59$). This suggests that the average payout announcement had a negative impact on the wealth of the target firm's shareholders. When the sample is split according to payout type substantial differences emerge. Share repurchases are associated with significantly negative abnormal returns averaging −1.62% ($Z = -7.02$) while special dividends typically increased the wealth of target firm shareholders by 2.66% ($Z = 4.34$). Nevertheless the difference is significant only at the 0.12 level ($t = 1.59$).

When the sample is further reduced by eliminating those firms with no other

[5] Specifically, market model parameters are estimated over a 240-day period beginning 280 days prior to the initiation of each control contest. Each abnormal return is standardized by its standard deviation to form a standardized abnormal return (SAR). These SARs, which are t-distributed, are then averaged across securities to obtain an average SAR which is assumed to be normally distributed under the Central Limit Theorem.

[6] As noted previously, this prior control activity takes many forms and is not restricted to formal takeover bids. For the sample studied in this paper, this prior activity had a substantial impact on shareholder wealth. Cumulative abnormal returns averaged 25.83% for the period beginning 40 days prior to the initiation of a control contest and ending 2 days prior to the defensive payout announcement for the forty contests with prior control activity. For the sample of nine announcements with no prior activity, cumulative abnormal returns averaged only 0.92% in the 40 days prior to the payout announcement.

Table III

Announcement Period Abnormal Returns

Two-day announcement period abnormal returns for the sample of 49 firms announcing defensive payouts in response to hostile corporate control activity over the period 1980–1987. Events with prior activity are those for which there has been some threat of a control change prior to the payout announcement. Clean events are those for which there are no other announcements during the two-day announcement period.

Panel A: Full Sample			
	Total Sample ($N = 49$)	Prior Activity ($N = 40$)	Clean Announcements ($N = 21$)
Mean Abnormal Return	1.88%	−0.83%	0.53%
Median Abnormal Return	1.72%	−0.58%	1.32%
Z-Statistic	6.72*	−2.59*	0.55
Percentage Negative ARs	42.9	52.5	42.9
Minimum Abnormal Return	−18.29%	−18.29%	−18.29%
Maximum Abnormal Return	40.62%	20.42%	20.42%
Panel B: Share Repurchases			
	Total Sample ($N = 40$)	Prior Activity ($N = 33$)	Clean Announcements ($N = 17$)
Mean Abnormal Return	0.60%	−1.62%	−1.45%
Median Abnormal Return	1.20%	−0.58%	−1.29%
Z-Statistic	1.41	−7.02*	−2.52*
Percentage Negative ARs	45.0	54.5	52.9
Minimum Abnormal Return	−18.29%	−18.29%	−18.29%
Maximum Abnormal Return	22.69%	8.90%	6.47%
Panel C: Special Dividends			
	Total Sample ($N = 9$)	Prior Activity ($N = 7$)	Clean Announcements ($N = 4$)
Mean Abnormal Return	7.55%	2.66%	8.94%
Median Abnormal Return	3.39%	2.88%	6.22%
Z-Statistic	13.61*	4.34*	6.45*
Percentage Negative ARs	33.0	42.9	0.0
Minimum Abnormal Return	−7.89%	−7.89%	2.88%
Maximum Abnormal Return	40.62%	20.42%	20.42%

* Denotes significance at the 1% level.

announcements during the two-day announcement period an even more striking difference emerges.[7] In this sample of 'clean' events, repurchases are associated with significantly negative abnormal returns of −1.45% ($Z = -2.52$) while special dividend announcements resulted in average abnormal share price increases of

[7] Note that this sub-sample is therefore a subset of the events with prior control activity. Even this sample of 'clean' announcements may be contaminated by other information releases. For example, the stock price reaction to the defensive payout announcement depends on the market's expectation regarding defensive tactics to be employed by the target firm. The payout may be viewed as value-increasing relative to other anticipated defensive tactics even if it is value-decreasing relative to the potential gains available through a transfer of control.

8.94% (Z = 6.45).[8] This difference in ARs is significant at the 0.01 level (t = 2.98).

B. Stock Returns Throughout the Control Contest

To gain additional perspective on the stock returns evidence, Table IV reports cumulative abnormal returns for various subperiods throughout the entire control contest. In addition, the sample is partitioned according to the eventual outcome of the contest. For each sample event both a contest initiation and contest outcome date are identified. Contest initiation is defined as the first indication in the *Wall Street Journal* of hostile control activity. This initiation occurred an average of 33 trading days prior to the payout announcement. The contest outcome date is a subjective estimate of the date at which the uncertainty as to whether control of the target would be transferred or not was resolved. Thus as of this date the conflict between the hostile bidder and the target was resolved *and* there were no public indications of other potential bidders. On average, there were 26 trading days between the announcement of a defensive payout and contest outcome.[9] The results show that in 28 of the 40 (70%) events with prior control activity, the target firm retained its independence following the announcement of the defensive payout. This rate exceeds that usually found around corporate control events. For example, in Dann and DeAngelo's (1988) sample of defensive restructurings, only one-third of the firms announcing restructurings retained their independence. Similarly, Jarrell (1985) noted that over 75% of target firms employing litigation as a takeover defense are eventually acquired.[10]

The cumulative returns evidence of Table IV suggests that, regardless of contest outcome, the presence of hostile control activity generates substantial increases in the wealth of target firms' shareholders. Prior to the announcement of defensive payouts, target firms experienced average CARs of 25.83% for the period beginning forty days before the control contest and ending two days prior to the defensive payout announcement.

[8] There appears to be an increase in the variance of returns during the announcement period. To account for this possibility, t-statistics were also computed using standard errors estimated from the cross section of announcement period abnormal returns. This reduces the significance of the abnormal returns in each sample. In panel A the t-stats are 1.33, −0.76, and 0.33 for the total sample, sample with prior activity, and clean sample, respectively. Similarly, the t-stats are 0.46, −1.53, and −1.02 in panel B and 1.50, 0.78, and 2.19 in panel C. While this procedure sacrifices statistical power, the results suggest caution in interpreting the Z-stats reported in Table III.

[9] These outcomes can be categorized into four primary groups: execution of the payout plan (16 cases), acquisition of the target firm (12 cases), greenmail payments (six cases), and withdrawal of takeover bid (15 cases). In three cases, the estimated outcome date fell after the expiration of a successful repurchase tender offer. So as not to bias the stock-returns evidence by including the repurchase offers' 'ex-dividend effect', these outcome dates were changed to the day before the expiration of the repurchase tender offer.

[10] The high rate of success in retaining target firm independence could be a result of the sample selection procedure. Since some events for which there has been no formal takeover bid are included in the sample, the success of the defense may reflect the fact that these firms never really were targets. To test this, the results were replicated using only the 36 firms that received a formal takeover offer. The results were nearly identical. Twenty-seven (75%) of the 36 firms remained independent following the announcement of the payout.

Table IV

Cumulative Abnormal Returns and Contest Outcomes

Cumulative abnormal returns (CARs) for various subperiods during the control contest for the sample of 40 announcements of defensive payouts with prior control activity. The sample is partitioned on the basis of contest outcome. The sample period is 1980–1987.

	40 Days prior to Initiation through 2 Days before Payout Announcement	Day before Announcement through Contest Outcome	40 Days prior to Initiation through Outcome
Total Sample ($N = 40$)			
Mean	25.83	−3.68	22.16
Median	28.63	−2.86	20.62
Z-Statistic	12.90*	−3.92*	10.18*
Frac. Negative	0.08	0.60	0.20
Incumbent Management Retains Control-Share Repurchase ($N = 22$)			
Mean	25.23	−9.51	15.95
Median	26.08	−6.05	13.58
Z-Statistic	9.57*	−9.55*	5.65*
Frac. Negative	0.09	0.82	0.23
Incumbent Management Retains Control-Special Dividend ($N = 6$)			
Mean	36.97	−6.05	30.09
Median	37.83	−3.26	30.22
Z-Statistic	6.16*	−1.65	4.35*
Frac. Negative	0.00	0.67	0.17
Hostile Bidder Acquires Control ($N = 3$)			
Mean	23.35	5.38	28.73
Median	29.43	4.09	26.57
Z-Statistic	3.27*	1.97	3.57*
Frac. Negative	0.00	0.33	0.00
Third-Party Acquires Control ($N = 9$)			
Mean	20.73	9.12	29.85
Median	24.74	13.03	37.29
Z-Statistic	5.22*	6.42*	6.81*
Frac. Negative	0.11	0.11	0.22

* Denotes significance of the CAR at the 1% level.

When stock returns are measured over the entire control contest, a different picture emerges. Firms which remained independent following repurchase announcements exhibit substantially lower CARs than those in which a control change took place. When the incumbent management team retained control, shareholders earned a cumulative abnormal return of 15.95% over the period extending from 40 days prior to initiation of the control contest through the contest outcome. In contrast, when the hostile bidder or a third-party obtained control the comparable CARs average 28.73% and 29.85%, respectively. These

CARs are significantly higher ($t = 1.83$) than those earned when control was not transferred. When combined with the pre-announcement price effects, this evidence suggests that the successful resistance to a takeover through a share repurchase is associated with large losses for the target firm's shareholders.

Further support for this view can be obtained by examining the stock price effects between the announcement of the defensive repurchase and the resolution of the control contest. The evidence in Table IV indicates that for those repurchases where the target firm eventually retained its independence, cumulative abnormal returns between the payout announcement and the contest outcome averaged −9.51%. In contrast, in both subsamples where control was transferred to another party, shareholders experienced positive CARs between the time of the defensive payout announcement and the contest outcome. The difference in CARs between those contests where the target remained independent and those where control was transferred is significant at the 0.01 level ($t = 3.27$).

This broader view of the stock price evidence provides some additional insight into the managerial motive behind defensive repurchases. The evidence does not support the hypothesis that the repurchase represents a higher-valued alternative to what is offered by the hostile party. Rather, the evidence supports the contention that the predominant motive for these payouts is the attempt to entrench the current management team. This interpretation is supported by a reading of the financial press which indicates that many sample firms also used other antitakeover measures typically associated with share price declines and interpreted by other authors as evidence of managerial entrenchment.[11] Specifically, during the control contest 23 firms initiated litigation against the potential acquirer, 10 firms issued either poison pill securities or other securities with special voting rights, 6 firms proposed greenmail payments, and 2 firms adopted antitakeover charter amendments. Furthermore, data from the *Investor Responsibility Research Center* (IRRC) indicate that target firms often had antitakeover devices in place prior to the contest. In particular, 7 firms had adopted fair price amendments, 10 had classified board provisions, and 18 had poison pill/blank check preferred plans prior to the sample control contest.[12]

An alternative interpretation of the stock returns evidence is that the negative CARs associated with those contests where target firms retained their independence are just the result of failed attempts by target managers to obtain a higher offer for the firm. Hence, while shareholders lose in an ex-post sense when an offer is resisted, a repurchase still may be in their interest ex-ante. However, this interpretation is difficult to justify in the sample studied here. First, if the repurchase is part of a bargaining strategy that is ex-ante in the shareholder's

[11] For example, see Jarrell (1985) for evidence on target litigation, Malatesta and Walkling (1988) and Rynegaert (1988) for evidence on poison pill issuances, Bradley and Wakeman (1983) and Dann and DeAngelo (1983) for evidence on greenmail payments, and Jarrell and Poulsen (1987) for recent evidence on supermajority provisions and classified boards.

[12] The *IRRC* publishes a yearly supplement summarizing those antitakeover devices adopted by Fortune 500 firms over the previous year. Since the first publication of this type was in 1984, the numbers stated above may actually understate the frequency of antitakeover devices used by the sample firms since for those events taking place prior to 1984 it cannot be determined whether or not the firm had a particular defense in place prior to the control contest.

interest, it should be associated with an average positive abnormal return. The evidence from Table III suggests that stock prices fell significantly following the typical repurchase announcement. Secondly, there is little evidence in the *Wall Street Journal* that managers attempted to promote an auction for their firm in an effort to secure the highest possible price.

Another explanation for the negative announcement effects is that a payout signals to the market the lack of higher valued alternatives. This explanation has been suggested by Mikkelson and Ruback (1988) and Shleifer and Vishny (1986) as a potential reason for the negative wealth effects associated with greenmail payments. However, this explanation also cannot be justified in the sample studied here. In those cases where a formal bid for control of the target was made, (36 cases), the blended premium averaged 36.4% over the pre-contest price of the target's shares.[13] Furthermore, for those firms remaining independent, the blended premium averaged 35.5%. This premium far exceeds the cumulative abnormal return earned by those firms remaining independent. Thus it appears that these firms clearly rejected a higher valued offer.

Interestingly, the same stock returns pattern does not exist for those firms that remained independent following the announcement of a special dividend. Full contest CARs average 30.09% for the special dividend firms. These cumulative stock returns are quite similar in magnitude to those contests in which the hostile bidder or a third party obtained control of the target firm. Furthermore, these firms displayed insignificant returns in the time between the announcement of the payout and the outcome of the contest.[14] These results are consistent with the interpretation that special dividend plans represent value-increasing strategies comparable to those offered through transfers of control. However it should be cautioned that much of the difference in full contest CARs between repurchases and special dividends appears to be driven by the stock returns prior to the payout announcement. Hence, the difference in full contest CARs may reflect differences in the potential gains from the contests themselves rather than from the different payout types.

III. Defensive Payouts and Contest Outcome

Although statistically significant, the announcement effects observed for the sample payouts are generally small in relation to the large positive cumulative abnormal returns observed over the entire control contest. This raises the question of the extent to which defensive payouts actually influence the sample control contests.

Table V provides evidence that the implementation of defensive payouts had an impact on the eventual contest outcomes. Of the 49 announced payouts, 37 were actually implemented by the target firms. When the payouts were eventually made, target firms generally remained independent. Only 3 of the 37 implemented

[13] The blended premium is conservatively estimated by assuming that the expected back-end value of any partial offer is equal to the pre-contest price of the target firm's shares.

[14] The average abnormal stock price decline during this period of 6.05% is relatively large in magnitude but is driven by one observation of −70.23%.

Table V

Payout Implementation and Contest Outcomes

Frequency of implementation of defensive payout plans for each control contest outcome. Percentages of subsamples in parentheses. The sample includes 49 announced payouts over the period 1980–1987.

Outcome of Control Contest	Number of Cases	Payout Plan Implemented	Payout Plan Not Implemented
Full Sample	49	37 (76%)	12 (24%)
Management Retains Control	37	34 (92%)	3 (8%)
Hostile Bidder Acquires Control	3	0 (0%)	3 (100%)
Third-party Acquires Control	9	3 (33%)	6 (67%)

payouts were followed by some transfer of control. In none of these cases did the original hostile bidder prevail. In contrast, control was transferred in 9 of the 12 cases where the payout was not implemented.[15] These results suggest that the payouts influenced contest outcomes to some extent. Consequently, the post-announcement CARs documented in Table IV can be plausibly linked to the payouts themselves. These CARs average −8.99% for those firms that implemented the announced payouts and 5.26% for those that did not implement the payout. Furthermore, in 17 cases the hostile bidding party publicly objected—usually through a court filing that sought injunctive relief—to the implementation of the defensive payout.

When viewed collectively with the small announcement period effects, these findings are consistent with the conclusion that defensive payouts contributed to the overall successful defensive strategy implemented by those firms that remained independent. The magnitude of the announcement effects implies that the payouts themselves were probably not sufficient to block the takeovers, but rather increased the probability of successful resistance.

An interesting question is whether there are links between various attributes of the defensive payouts, contest outcomes, and the associated stockholder wealth effects. To address this question, Table VI examines each nominal type of payout (where known) according to the average size of the payout as a percentage of the target firm's pre-contest value, the eventual outcome of the control contest, and the two-day announcement period abnormal return.

Table VI indicates that there were large differences in payout size across the various types of transactions. Special dividend plans involved substantially larger payouts than any of the other types, averaging 104.6% of the target's equity value two months prior to the control contest. At the other extreme, the average relative size of open-market repurchases was only 12.37%.

[15] These results were also replicated using only the 36 firms that received a formal takeover offer. Only 2 of the 27 firms implementing a payout plan remained independent while 7 of the 9 firms that did not implement the announced plan were eventually acquired.

Table VI

Relative Size, Wealth Impacts, and Contest Outcomes

Relative size, wealth impacts, and contest outcomes for the sample of 49 announcements of defensive payouts over the period 1980–1987. Type of payout (where available) is determined on the basis of the initial announcement of the defensive payout as reported in the *Wall Street Journal Index*. Relative transaction size is defined as the dollar value of the defensive payout as a percentage of the targets equity value two months prior to the control contest. The announcement period abnormal returns are reported for the 21 clean announcements only. These include 3 open-market repurchases, 10 repurchase tender offers, 4 exchange offers, 0 unknown repurchases, and 4 special dividends.

Type of Payout	Number of Cases	Mean (Median) Relative Size	Number (%) of Targets Acquired	Mean (Median) Announcement Period Abnormal Return
Full Sample	49	44.69% (34.00%)	12 (25%)	−0.53% (1.32%)
Open-Market Repurchases	10	12.37% (11.46%)	2 (20%)	(−0.84%) (1.32%)
Repurchase Tender offers	16	38.23% (33.14%)	5 (31%)	−2.25%* (−1.58%)
Exchange Offers	7	50.81% (36.59%)	3 (43%)	0.08% (0.15%)
Unknown Repurchase Type	7	22.43% (21.50%)	1 (14%)	
Special Dividends	9	104.60% (117.91%)	1 (11%)	8.94%* (6.22%)

* Denotes significance of the mean abnormal return at the 1% level.

There appears to be little systematic relationship between the contest outcome and either the payout type or the relative payout size. An exception to this general statement may be the special dividend plans. In only one case where a special dividend was announced was the target eventually acquired by another firm. In this case the dividend plan was not implemented. This suggests that special dividends may provide a marginally stronger deterrent to a hostile takeover attempt. Note, however, that all payout types appear to be relatively strong deterrents since 76% of the firms announcing defensive payouts retained their independence.

Table VI also documents evidence on the wealth effects of each payout type. Although the limited sample sizes make statistical inference somewhat problematic, the results show that both open-market repurchases and repurchase tender offers were associated with negative abnormal returns. There appears to be little relationship between the size of the payout and the announcement period stock returns in the share repurchase group. In fact, the simple correlation between relative payout size and announcement period return for this group is just 0.01.

IV. Evidence of Shifts in Corporate Policy

The evidence on the wealth effects of defensive payouts shows that regardless of payout type, target firms exhibited positive cumulative abnormal returns when

measured over the duration of the control contest. This suggests the possibility that targets implement value-increasing structural changes that are related to or coincident with the defensive payout.[16] This section reports on the nature of some possible structural changes.

A. Changes in Capital/Ownership Structure

Table VII presents a comparison of leverage ratios and managerial vote ownership percentages for the period just prior to the control contest and just after the outcome of the contest for the 37 firms that retained their independence. Columns (1) and (2) show a dramatic increase in the ratio of long term debt to total assets in the post-outcome period. The average debt ratio increased from 21.0% in the pre-contest period to 42.6% in the post-outcome period. This increase was widespread; 27 of the 37 firms increased the ratio of debt to equity in their capital structure. Furthermore the change in debt ratio appears to have been the result of an increase in debt rather than a reduction in assets. The average book value of debt more than doubled from \$594.8 million to \$1286.5 million while total assets remained essentially unchanged.

Similarly, 21 firms increased the beneficial ownership of voting rights by managers and directors following the control contest. Only five firms exhibited a decrease in managerial ownership.[17] Average managerial ownership increased from 5.0% in the pre-contest period to 11.2% in the post-outcome period. Panels B and C show that these changes in capital and ownership structure were generally more dramatic for those firms that announced special dividend plans. Average leverage ratios increased from 22.0% to 61.5% for these firms while managerial ownership of voting rights increased from 5.6% to 18.9%.

Such changes in capital and ownership structure can have valuation consequences. Jensen (1986a, b) and Stulz (1990) argued that increased debt can play a valuable role in reducing agency costs. By increasing the amount of debt in its capital structure, the firm can effectively limit the amount of managerial discretion over investment decisions. Firm value can be enhanced by a reduction in the number of negative net present value projects taken by the firm.

Increased debt can also provide incentives for enhanced productive efficiency. With high levels of debt, managers have the incentive to reduce inefficiencies within the firm in order to avoid the costs associated with bankruptcy. Consistent with this conjecture, Kaplan (1989) documented significant post-buyout operational efficiencies for a sample of firms which went private through highly leveraged management buyouts.

Increased managerial ownership of cash-flow rights can also play a role in aligning the interests of managers and shareholders. Jensen and Murphy (1988)

[16] Another possibility is that the market expects the target firm to be 'put in play' again in the near future. Therefore the positive CAR merely reflects some expectation of a future control premium. This would be similar to Bradley, Desai, and Kim's (1983) evidence on unsuccessful tender offers. This issue is explored in further detail in Section IV.C.

[17] In those cases where both the pre-contest and post-outcome ownership levels are below 1%, the case is recorded as no change in managerial ownership. Since this occurs 9 times, only 26 of the 35 cases where data are available have changes in the ownership structure recorded. Appendix B lists the changes in capital/ownership structure for each of the 37 firms remaining independent.

Table VII

Changes in Capital and Ownership Structure

Actual changes in leverage and managerial ownership of voting rights for the 37 firms remaining independent after a defensive payout announcement over the sample period of 1980–1987. Leverage is defined as the ratio of long-term debt to total assets as listed in *Moody's Manual.* Managerial ownership is defined as the beneficial ownership of all officers and directors as stated in the firm's proxy statement. A *t*-statistic tests for differences in the means of the leverage and ownership variables using a paired comparisons test.

	Leverage		Managerial Ownership	
	Before	After	Before	After
A. Full Sample ($N = 37$)				
Mean	21.0	42.6	5.0	11.2
Median	16.5	32.4	1.7	2.7
t-Statistic		4.6		3.5
B. Share Repurchases ($N = 29$)				
Mean	20.7	37.4	4.8	9.1
Median	16.4	35.0	1.7	2.7
t-Statistic		4.3		2.4
C. Special Dividends ($N = 8$)				
Mean	22.0	61.5	5.6	18.9
Median	14.6	32.4	1.5	13.5
t-Statistic		2.2		2.8

documented a surprisingly low relationship between firm performance and executive compensation. They argue that this reduces the incentive for top management to maximize firm value. By increasing managers' fractional ownership of cash flows, the pay/performance relationship can be strengthened and thus improve the incentive structure of the firm.

On the other hand, increasing managerial control of voting rights can effectively insulate managers from the external control market. This tradeoff between the alignment of interests and managerial entrenchment was emphasized in the model of Stulz (1988). Morck, Shleifer, and Vishny (1988) examined the relationship between firm performance and board ownership and found evidence of a nonmonotonic relationship. For ownership levels below 5%, firm performance increased through an increase in board ownership. However, between ownership levels of 5% and 25%, firm performance declined as ownership increased. This evidence suggests that managerial entrenchment can occur at levels of ownership as low as 5%.

For the sample of firms which remained independent after defensive payouts, 26 of the 37 had pre-contest ownership levels below 5%. Thus, based on Morck, Shleifer, and Vishny's results, the majority of these firms could potentially have increased firm performance through an increase in managerial ownership. However, in seven cases, target firm managers increased their control of voting rights

without concurrently increasing their cash flow ownership.[18] Thus, while voting rights control increased from 5% to 11.2%, ownership of cash flows only increased from 3.9% to 5.3%. The separation of cash flow ownership and voting rights control was similar to that which takes place in dual-class recapitalizations. Jarrell and Poulsen (1988) documented negative wealth effects associated with announcements of dual-class recapitalizations and argued that their results 'highlight the ability of insiders with large shareholdings to further protect themselves from hostile takeovers'.[19]

B. Top Management Turnover

The takeover market can be viewed as one of the mechanisms through which managers are encouraged to take actions that are in the best interests of shareholders. Viewed in this manner, the takeover market complements such internal mechanisms as the board of directors, internal labor market competition, and monitoring by large shareholders. Recent empirical evidence suggests that top management turnover is related to firm performance. Both Warner, Watts, and Wruck (1988) and Weisbach (1988) found a significant inverse relation between a firm's stock price performance and the likelihood of a top management change. These results provide support for the effectiveness of internal monitoring mechanisms.

When internal mechanisms are not effective, the external takeover market may be needed to discipline poor management teams. However, if a firm can effectively reject a value-increasing bid through a defensive payout, the management team may be able to insulate itself from the discipline of the external control market. To examine this issue, turnover in the top management team in the three years following a control contest is explored. For this purpose, a top management change is defined as a change in either the president, chief executive officer (CEO), or the chairman of the board as reported in the *Wall Street Journal*.[20]

[18] In these seven cases (Colt, Diamond Shamrock, Grumman, Harcourt Brace Jovanovich, NL Industries, Phillips Petroleum, and Standard Brands), this is accomplished primarily through the use of retirement plans such as ESOP and PAYSOP plans. Since in many cases target firm managers are the trustees of a plan, when the plan does not receive the defensive payout its fraction of outstanding shares increases, thereby increasing the voting power of the managers. In these 7 cases managerial control of voting rights increased from 5.7% to 29.2% while their ownership of cash flow rights only increased from 3.1% to 3.5%.

[19] In Stulz's (1988) model, the market reaction to changes in ownership structure depended on the current ownership structure. However, there are empirical problems in testing the model with the sample of payouts used here. First, as noted previously, the market reaction to a payout announcement will be conditioned on the presence and the strength of other anticipated defensive tactics employed by the target firm. Second, it is often not clear at the time of the announcement what impact the proposed payout will have on the firm's ownership structure. This will depend on both the type of payout made and management's participation in the payout. Often neither of these are known at the time of the announcement. Noting these difficulties, it is probably not surprising that a regression of announcement-period abnormal returns on ownership-structure variables did not yield significant results.

[20] Similar definitions of top management can be found in DeAngelo and DeAngelo (1988), Klein and Rosenfeld (1988), and Warner, Watts, and Wruck (1988).

Table VIII

Top Management Turnover

Cumulative turnover in top management control for the sample of 37 firms in which management retained control through the outcome of the control contest and for the full sample of 49 firms announcing defensive payouts over the sample period of 1980–1987. Top management turnover is defined as a change in the president, chairman, or CEO of the target firm. It is assumed that there is turnover in top management control in those 12 cases where either the hostile bidder or some third party acquires control of the target firm.

	As of Contest Initiation	Between Initiation and Outcome	First Year after Outcome	Second Year after Outcome	Third Year after Outcome
A. Management Retains Control ($N = 37$)					
Number of Firms	0	2	13	17	20
Percentage of Subsample	0%	5.4%	35.1%	46.0%	54.1%
B. Full Sample ($N = 49$)					
Number of Firms	0	14	25	29	32
Percentage of Subsample	0%	28.6%	51.0%	59.2%	65.3%

Table VIII documents the cumulative percentage of firms that experienced top management turnover in the period beginning with the initiation of each control contest and ending three years after the outcome of the contest. The results show a substantial rate of turnover. Between the initiation of the contest and one year after the outcome, 35.1% of the subsample of firms that remained independent experienced some managerial turnover. Within three years after contest outcome, over half (54.1%) of such firms had some change in their top management team.[21] When the 12 firms that experienced some change in control are added to the 37 firms that remained independent in panel B, the results show that within three years of contest outcome, 65.3% of the sample firms subjected to some hostile control activity had a change in the top management control of the firm's resources.

These numbers strongly suggest an association between the control market and abnormally high rates of top management turnover. The turnover rates documented in Table VIII are substantially higher than the normal rates of managerial turnover documented in Warner, Watts, and Wruck (1988) and Weisbach (1988).[22] Furthermore they are significantly higher than the 10.8% of sample firms that experienced turnover in the year prior to contest initiation. However, the numbers are strikingly similar to other studies of managerial turnover surrounding control contests. DeAngelo and DeAngelo (1989) studied the incidence of top management changes subsequent to proxy contests where dissidents did not acquire board control. They found that 51.3% of their sample firms had some change in top management in the three years following the

[21] These numbers understate the incidence of top management changes since in those cases where the contest outcome is after 1986, there is not 3-years worth of available post-outcome data.

[22] Warner, Watts, and Wruck (1988) report an average annualized rate of change in top management of 11.5% while Weisbach (1988) reports an average CEO departure rate of 4.8%, excluding those departures where the CEO is of retirement age.

outcome of the proxy contest. Similarly, Klein and Rosenfeld (1988) examined top management changes following greenmail payments. They found that 40.2% of their sample firms experienced top management turnover in the two years following the greenmail payment.

This evidence indicates that there was some link between the external and internal control markets that brought about abnormally high rates of managerial turnover even in those cases where management successfully retained control over the challenge of some hostile party. The proximity of the turnover to contest outcomes and the link between contest outcomes and the implementation of defensive payouts suggests a connection between the payout and the abnormal turnover. The results of Table VIII are consistent with the joint hypothesis that defensive repurchases are not in the shareholder's interest, *and* the target firm's internal mechanisms provide sufficient monitoring of these managerial actions. However, it should be cautioned that the high turnover rate cannot be attributed *solely* to the defensive payout since, as noted previously, managers take many other defensive actions during the control contest as well.

Another plausible explanation is that the payouts and the associated debt burden may require a restructuring of the firm for which the current management team does not possess the necessary skills. This explanation may be particularly appropriate in the three cases where managerial turnover followed the implementation of a special dividend plan.

C. Corporate Downsizing/Asset Restructuring

This section reports the incidence of other types of corporate policy changes announced by those firms that remained independent after announcing a defensive payout. The *Wall Street Journal Index* was examined for the year following the outcome date of each firm-control contest. Based on a careful reading of these entries, announcements fitting into six major categories are recorded for each firm. These categories are: sale of the firm, purchase of a significant block of shares by an outside party, divestiture program, sale of a major unit, plant closing, and employee layoff/early retirement program.

Table IX presents a broad overview of the types of corporate restructurings announced by the 37 firms after the outcome of the control contest. Categories (1) and (2) indicate that a total of 11 firms appear to have remained strong candidates for some transfer of control. Of these 11, 2 firms were eventually sold while the remaining 9 had some indication of interest expressed by an outside party. This interest came in the form of either a formal takeover proposal (four firms) or the purchase of a significant stake (five firms). These observations provide another plausible explanation for why the stock prices of those firms that remained independent stayed at a level that was significantly higher than pre-contest levels. It may be that the post-outcome price reflected some expected control change premium based on the market's probabilistic assessment of a future change in control. However, it does not appear likely that this can completely explain the positive stock price effects. The full-contest CARs for the 11 firms that remained 'in-play' are not significantly different from those of the remaining firms. For the 11 'in-play' firms, the average CAR for the period that

Table IX

Corporate Restructuring Activity

Types and incidence of corporate restructurings undertaken by 37 firms remaining independent after the announcement of a defensive payout over the period 1980–1987. Restructurings are announced during the year after the outcome of each control contest.

Restructuring Type	Number of Firms	Percentage of Firms
1. Firm Sold or Liquidated	2	5.4%
2. Purchase of Significant Stake/ Formal Takeover Offer for Firm	9	24.3%
3. Firm Announces Divestiture Program Related to Defensive Payout	13	35.1%
4. Sale of Major Units	11	29.7%
5. Plant Closings	2	5.4%
6. Employee Layoffs/Early Retirement Programs	11	29.7%

began 40 days prior to initiation and ended at contest outcome is 17.74%. This compares to 18.42% for the other 26 firms that remained independent. Thus, either the market could not distinguish those firms that would remain 'in-play' or the other 26 firms initiated some structural changes that were expected to increase firm value. The evidence presented below seems to support the latter explanation.

Categories (3) and (4) in Table IX provide evidence of corporate downsizing in the post-outcome period. Thirteen of the 37 firms announced some type of asset restructuring program that involved wholesale divestitures. In every case, the divestiture program was directly related to either the defensive payout or the debt load taken on by the firm in fighting off a hostile bidder. Another 11 firms announced the sale of a major unit(s) in the year after the outcome of the control contest. Thus, 24 of the 37 firms that remained independent announced asset restructurings which effectively reduced the amount of corporate assets under the control of the target firm's management team.[23] These results were even more dramatic for the firms that announced special dividends. Seven of these eight firms announced restructuring programs that consisted of large-scale divestitures.

These findings are particularly interesting given the public outcry against hostile takeovers. A frequent criticism of the hostile takeover process is that 'corporate raiders' engineer 'bust-up takeovers' by purchasing the shares of

[23] It is difficult to quantify the reductions in assets and debt load since the timing of the sample transactions severely limits the amount of post-contest data. However, for the 19 transactions for which there is year-end data for the year after the outcome of the control contest, there is some evidence of both asset and debt reductions. The book value of total assets declines from an average of $3914 million to $3619 while the average debt-total assets ratio falls from 45.9% to 42.6%. While these reductions are relatively small (7.5% and 7.2%, respectively), they clearly understate the impact of the restructuring since much of the restructuring is not implemented within the year after contest outcome.

target firms and then selling off the firm in piecemeal fashion. The evidence in Table IX indicates that asset sales appear to be an eventual outcome of the takeover process even if the incumbent management team retains control of the target firm. Thus, it is entirely plausible that the incumbent managers implement some of the value-increasing corporate policy changes that the hostile party would have implemented had control been transferred.

Categories (5) and (6) document the incidence of announcements which reduced the corporate payroll. The evidence suggests that firms generally do not completely shut down operations in manufacturing plants but frequently attempt to reduce labor costs through employee layoffs or voluntary early retirement programs. Only two firms announced plant closings in the year after the outcome of the control contest. However, 11 of the 37 firms that remained independent announced some employee reductions. This number is subtantially higher than the number of firms (four) that announced similar plans in the year prior to the control contest. Furthermore, these reductions were often linked to the control contest through the target firm's general restructuring program. Firms often quoted their heavy post-payout debt load as motivation for reducing payroll costs.

Overall, the evidence in Table IX suggests that target firms initiate substantial restructurings of their assets after defeating a hostile bidder. These restructurings primarily take the form of large-scale divestiture programs which significantly streamline the operations of the firm. As part of the general downsizing effort, target firms often also offer incentives for employees to retire early, thereby further reducing costs. It is worth noting that since voluntary corporate sell-offs are typically associated with increases in shareholder wealth,[24] it is likely that these restructuring programs enable target firm managers to increase the value of the firm relative to its pre-contest value. This conjecture is supported by the fact that those firms making restructuring decisions of the type in Table IX experience full-contest CARs averaging 20.75% while those without restructuring announcements average 12.72%. However, this difference is not significant at the 0.10 level ($t = 1.09$). The higher incidence of restructurings for those firms that announced special dividends provides a plausible explanation for the higher CARs associated with these firms.

V. Summary and Conclusions

This study investigated the use of defensive changes in corporate payout policy as a means of retaining the independence of a target firm during the course of a hostile control contest. The evidence indicates that announcements of defensive repurchases are, on average, associated with negative changes in the wealth of target firm shareholders. The repurchases are often part of an overall defensive strategy undertaken by the target firm and are associated with a high rate of success in maintaining target firm independence. However, in the process of

[24] For example, Hite, Owers, and Rogers (1987) reported significant positive abnormal returns to shareholders of firms that announced voluntary sell-offs and Kim and Schatzberg (1987) found significant positive abnormal returns for firms that announced voluntary liquidations.

retaining this independence, target firm shareholders suffer large abnormal wealth losses. Furthermore, the result of many payout plans is the concentration of managerial control of voting rights without a simultaneous increase in managerial cash flow ownership. This evidence can be interpreted as consistent with managers using the defensive strategy for their own benefit at the expense of shareholders. An exception to this general interpretation appears to be the use of special dividend plans. While also associated with a high rate of success in maintaining target firm independence, these payouts are typically associated with abnormal wealth increases for target firm shareholders.

Cumulative abnormal returns for the entire control contest indicate substantial wealth gains for target firm shareholders even when a transfer of control is not effected. Thus, although the announced payouts typically decrease shareholder wealth relative to the expected payment from the hostile bidder, they increase shareholder wealth relative to its pre-contest value. A possible explanation for this phenomenon is that the market expects value-increasing changes in the target firm to occur in the future. The evidence from Section IV supports this view in that it documents major structural changes in target firms subsequent to successful takeover defenses. As a result of the defensive payouts, both the target firm's capital structure and the structure of voting rights are dramatically altered. These changes may improve managerial incentives to maximize firm value. Furthermore, there is an abnormally high rate of top management turnover in the 3 years following the control contest. This indicates that managers are not able to insulate themselves completely from the discipline of the external control market.

Managers implement major strategic changes in the target firm as a result of the control contest. Many firms engage in programs designed to sell off major lines of business in an effort to streamline operations and help service the additional debt taken on during the control contest. Firms also take steps such as employee layoffs and early retirement programs that are intended to reduce corporate overhead costs. These structural changes are generally more dramatic for those firms announcing special dividends, suggesting a possible explanation as to why these firms exhibit substantially higher cumulative stock returns over the entire control contest. Nevertheless, it is unclear whether special dividends per se play a unique role in bringing about these changes or whether repurchases of the same magnitude would result in the same outcome.

This overall evidence suggests that the external market for corporate control exerts some discipline on corporate managers even in those cases where managers have defeated a hostile bidder. A reasonable interpretation of the evidence is that in resisting a hostile offer managers undertake actions which will not only defeat the bidder but also insulate themselves from future control changes. These actions include not only those which would appear to be purely entrenchment oriented, such as the concentration of voting power in friendly hands, but also those that are value-increasing, thereby reducing the profitability of an external control change. These restructurings can be viewed in many cases as a compromise between the higher-valued offer of the hostile party and the lower-valued operating strategy of the target firm prior to the control contest.

Appendix A

Firms announcing defensive payout plans during the period 1980 through 1987.

Firm Name	Announcement Date (year, month, day)	Firm Name	Announcement Date (year, month, day)
Allegis	870529	GTE Corp.	861107
Anderson Clayton	860825	Harcourt Brace Jovanovich	870527
Ashland Oil	860403		
Barnes Group	871208	Harsco	810227
Burlington Industries	870512	Holiday Corp.	861113
Caesar's World	870406	Litton Industries	850528
Carter Hawley Hale	840418	Lucky Stores	861013
Carter Hawley Hale	861209	National Can	850220
CBS	850705	Newmont Mining	870922
Colt Industries	860721	NL Industries	860415
CPC International	861105	Owens Corning	860829
Curtiss Wright	801229	Phillips Petroleum	841224
Dan River	821123	Phillips-Van Heusen	870731
Dayton Hudson	871022	Pogo Producing	830428
Diamond Shamrock	861204	Potlatch	851112
FMC	860224	Revlon	850821
GATX	860516	Richardson-Vicks	850925
Gelco	860827	Sperry	860515
General American Oil	821223	Standard Brands Paint	871111
GenCorp	870407	Storer Communications	850423
Gillette	861125	Telex	871106
Golden Nugget	870904	Union Carbide	851216
Goodyear	861107	Unocal	850417
Graniteville	830516	USG	861121
Grumman	811014	Warnaco	860324

Appendix B

Changes in Leverage and Ownership Structure

Actual changes in leverage and managerial ownership of voting rights for 37 firms remaining independent after a defensive payout announcement. Leverage is defined as the ratio of long-term debt to total assets as listed in *Moody's Manual.* Managerial Ownership is defined as the beneficial ownership of all officers and directors as stated in the firm's proxy statement. NA indicates that data item was not available. The sample period is 1980–1987.

	Leverage		Managerial Ownership	
	Before	After	Before	After
Allegis	18.3	NA	1.0	1.0
Ashland Oil	15.3	18.5	2.0	1.6
Barnes Group	11.6	24.8	25.0	NA
Caesar's World	37.5	6.8	2.0	2.0
Carter Hawley Hale	20.4	20.4	5.0	8.4
Carter Hawley Hale	17.9	32.4	4.8	15.3
CBS	11.4	94.5	6.7	8.3
Colt Industries	27.3	143.5	10.9	39.8
CPC International	16.4	22.1	1.0	1.0
Curtiss Wright	15.3	14.5	NA	3.9
Dayton Hudson	23.6	27.7	1.0	1.0

Appendix B—*Continued*

	Leverage		Managerial Ownership	
	Before	After	Before	After
Diamond Shamrock	31.6	44.1	0.6	1.0
FMC	11.3	66.6	19.0	51.7
GATX	34.8	39.9	1.3	2.7
Gelco	71.6	NA	12.6	30.6
GenCorp	9.8	42.7	3.4	1.0
Gillette	18.0	36.0	1.4	1.5
Golden Nugget	63.3	NA	17.9	29.3
Goodyear	12.3	32.3	0.7	0.2
Grumman	25.5	35.0	1.7	18.4
GTE	15.3	32.4	0.1	1.0
Harcourt	46.2	111.3	5.6	29.6
Harsco	19.2	17.8	1.8	1.7
Holiday	8.9	28.7	1.0	11.6
Litton	5.2	79.8	3.2	6.5
Lucky Stores	12.4	9.1	1.5	0.7
NL Industries	21.9	16.0	1.0	51.1
Newmont Mining	8.6	41.1	0.1	0.3
Owens Corning	23.0	75.2	1.0	2.7
Phillips Petroleum	14.1	46.6	0.2	6.9
Phillips Van-Heusen	1.6	36.9	16.4	18.7
Pogo Producing	39.1	30.9	4.1	5.7
Potlatch	26.1	30.1	13.3	16.7
Standard Brands	2.4	71.6	1.3	21.0
Union Carbide	16.5	40.4	1.7	0.3
Unocal	15.9	51.1	1.0	1.0
USG	7.5	25.7	0.9	1.0

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