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Stock Repurchase as a Defense against Hostile Takeovers

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Abstract

The board of directors has the authority to decide on the sale of the company's own stocks, and the board of directors' decision to duly dispose of the company's own stocks that have been legitimately acquired should, in principle, be deemed lawful. Even when the company sells its own shares for the defense of the management right, the legality of such sale should be determined considering the reasonable basis and proportionality of the defensive action. If the decision to sell the company's own shares to its shareholders or to third parties is subject to the business judgment of the board of directors, the legality of such sale should be determined in accordance with the same principle. The board of directors' decision to sell the company shares should thus be determined in accordance with the principle of reasonable basis and the principle of proportionality. However, if the purpose of the sale of the company shares is only for the benefit of the controlling shareholder having the management right, rather than for the benefit of the company and the shareholders as a whole, then it may be possible for such sale to be deemed illegal. The sale of the company's own shares per se *should not be considered an automatic violation of the principle of shareholder equality. Nevertheless, if the company's own shares are sold to certain major shareholders at a price that this significantly lower than the market price, such sale may be in violation of the principle of shareholder equality or the directors' duty of care as the fiduciary of the shareholders.*

I. Introduction: Defending against Hostile Takeovers

The term "mergers and acquisitions" (M&A) is generally understood as referring to a transaction that aims for control of management.[1] Among different types of M&As, a hostile takeover presupposes an adverse relationship between the current board of directors of the target company and

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1) JAE-YEOL KWON, DEFENSIVE TACTICS AGAINST HOSTILE TAKEOVERS 5 (KOSDAQ Listed Companies Association, April 2005).

the hostile company trying to acquire the target company.

In the event of a hostile takeover attempt, the management of the target company can use defense strategies involving the acquisition of company shares or the amendment of articles of incorporation. Examples of defense strategies involving the purchase of the target company's shares include: (i) acquisition of shares for control; (ii) securing of a friendly shareholder for mutual cooperation; (iii) repurchase and sale of the company's own shares; (iv) paid-in capital increase through a designated third party; (v) issuance of convertible securities to friendly parties; (vi) issuance of bonds with warrant to friendly parties; (vii) use of a white knight; and (viii) large-scale paid-in capital increase. Defense strategies involving the amendment of articles of incorporation include: (i) amendment of provision relating to issuance of new shares to a third party; (ii) adoption of staggered board system; (iii) tightening of director qualifications; (iv) tightening of requirements for appointment of director; (v) adoption of a special majority rule; (vi) inclusion of a golden parachute; (vii) limitation on use of proxy votes; and (viii) exclusion of cumulative voting system. In addition to these two types of defense measures, the target company may use strategies involving operational management, other specific defense activities (e.g., sale of material assets and report or alerting to the regulatory authorities of the aggressor company's violation of disclosure duties, procedural regulations or any other such laws or regulations), and the prescription of poison pills.[2]

A hostile takeover can have both positive and negative effects. On the positive side, a hostile takeover can reduce the agency problem, enhance efficiency in management, and increase social and economic wealth. On the negative side, a hostile takeover can transfer wealth from, or reduce the wealth of, shareholders and bring a myopic attitude to operational planning.[3] Accordingly, whether or not a hostile takeover is justifiable depends on whether it produces more positive results than negative ones.

The target company's stock repurchase[4] and the sale of the target

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2) *Id*. at 55; Hwa-Jin Kim, *Current Status of the M&A Market and Challenges in the Areas of Policy and Law*, 6 BUSINESS, FINANCE & LAW 31 (July 2004) (in Korean); DALE A. OSTERLE, MERGER AND ACQUISITIONS 231.

3) JAE-YEOL KWON, *supra* note 2, at 30.

4) Hwa-Jin Kim, *supra* note 3, at 44.

company's own stocks to a third party have generally been accepted as legally permissible ways of defending against hostile takeover attempts. However, the legality of these defense strategies came into question with a preliminary disposition and the subsequent final holding on a case before the Seoul Western District Court in 2006, involving a hostile takeover situation. In that case, the Court held that the target company's over-the-counter sale of stocks to the controlling shareholder, serving as the representative director of the company, and other persons in special relationship with the controlling shareholder were illegal because such sale violated other shareholders' rights under the principle of shareholder equality. In light of this new development, the following sections examine legal issue relating to defense strategies against hostile takeover attempts, including issues involving the sale of the target company's treasury shares.

II. Defense Strategies against Hostile Takeovers and Duties of Director

1. Legal Principles on Director's Duties

Under the Anglo-American legal system, a director of a company must act in compliance with the principles of duty of care and duty of loyalty. Under the principle of duty of care, the director must exercise the care that a reasonable person would use under similar circumstances, and the director may be held responsible for her action or inaction during the performance of her duties.

The duty of loyalty, on the other hand, requires the director to act in the best interest of the company,[5] and in the event of a conflict between the interest of the director and the interest of the company, the director must put the company's interest ahead of her own. To determine whether a director has breached her duty of care, the Court applies the doctrine of business judgment, and for determination on the director's violation of duty of loyalty, the principle of fair dealing is applied.

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5) Arthur R. Pinto, Understanding Corporate Law § 8.01.

The Commercial Act of Korea characterizes the relationship between the company and its director as an agency relationship requiring the director to perform her duty as a fiduciary of the Company (Commercial Code, Art. 382(2); Civil Act, Art. 681) and in accordance with laws and regulations and the company's articles of incorporation (Commercial Act, Art. 382-3). Accordingly, if the director violates her duty as a fiduciary or the duty of loyalty, and the company suffers damages as a result, then the director may be held liable for the damages (Commercial Act, Art. 399(1)). Moreover, in the event the company incurs an irreparable damage as a result of directors' action in violation of law, regulations or the articles of incorporation, the shareholders may bring a derivative action against the directors (Commercial Act, Art. 402). One peculiar aspect of the Korean law that is that a director may be criminally charged with malfeasance under the Act on the Aggravated Punishment, Etc. of Specific Economic Crimes.

2. Duties of Director and Defense against Hostile Takeovers

No consensus has been reached in legal communities over whether directors of the target company may actively intervene to defend their management control against a hostile takeover attempt.[6] Under the American legal system and Korea's majority view, directors are, in principle, permitted to defend their management, using their business judgment, and directors are held responsible for any abuse of their power committed in their defense efforts.[7] To qualify as a legitimate business judgment in the Korean legal system, the following elements must be shown: (i) directors' judgment on a business matter; (ii) disinterestedness and independence of directors; (iii) a judgment based on sufficient information; (iv) good will; (v) absence of abuse of discretion; (vi) absence of fraud, illegality, abuse of authority, and waste of company assets.[8] Directors must also consider all reasonably accessible

6) Wook Rae Lee, *Legal Assessment of Director's Defense Tactics against Hostile Takeovers*, 12 BUSINESS, FINANCE & LAW 10 (July 2005).

7) Jong Joon Song, *Business Judgment Rule and Issues of Its Acceptance in Korea*, 364 HUMAN RIGHTS AND JUSTICE 23 (December 2006).

8) Seok-Bum Hong, *Application of Business Judgment Rule and its Limits*, 364 HUMAN RIGHTS AND JUSTICE 26 (December 2006).

material information before making any business judgment in relation to the sale of the company. Particularly, before deciding on a matter relating to an M&A transaction, directors have the duty of care as fiduciary of the company to collece all necessary information and to act with caution.[9] Directors must not leave such decision to the shareholders without taking any position on the matter. In the event that directors have to approve a transaction between the company and a director, the directors must show that the transaction is fair to both parties.[10] If the directors are given the authority to decide whether to sell the management control to a hostile company or to a white knight, the directors' role shifts from the protector of management control to a seller at an auctioneer who must sell the company to the highest bidder to maximize shareholders' profit.[11]

In defending the target company, the following two conditions must be satisfied for the doctrine of business judgment to apply: (i) a reasonable belief that there was a risk to the policy and efficacy of the company (i.e., the "principle of reasonable basis"); and (ii) reasonableness of the defense measures taken in relation to the degree of risk posed (i.e., the "principle of proportionality").[12] Once the above two conditions are shown to be satisfied, directors are protected under the doctrine of business judgment.

To satisfy the principle of reasonable basis, the board of directors must have in good faith decided, after examining the degree of threat, that it was necessary to use the defense measures the board decided to employ. If the Court recognizes that the use of the defense measures was appropriate, the directors' decision to use such measures will be deemed a valid business judgment. To hold the directors responsible, shareholders must prove that the directors violated their fiduciary duty by showing, among others, that (i) the directors' objective was to maintain their position in the company; (ii) the directors did not act in good faith or committed fraud; and (iii) the directors

9) Smith v. Van Gorkom, 488 A.2d. 858 (Del. 1985).
10) Weinberger v. UOP Inc., 457 A.2d. 701 (Del. 1983).
11) Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d. 173 (Del. 1985).
12) Unocal Corp. v. Mesa Petroleum Co., 493 A.2d. 946 (Del. 1985).

lacked adequate information on which they could base their decision.[13] Even when the directors' decision is not protected under the doctrine of business judgment, it is sometimes justified under the principle of equity.[14] In the event the directors have to choose between two potential acquirers, the directors' decision may be protected if it satisfies the principle of reasonable basis and the principle of proportionality.[15] When there is change of management, the directors must in good faith take actions based on reasonably reliable information, actively engage in negotiations with the potential acquirers, and treat all potential acquirers on equal basis.[16]

III. Repurchase and Sale of Company's Own Shares for the Defense of Management Control

1. Stock Repurchase for the Defense of Management Control

Prohibiting stock repurchase in principle, the Commercial Act permits a company to buy back its own shares only for certain purposes such as the cancellation of stocks (Commercial Act, Arts. 341, 341-2 and 342-2). On the other hand, the Financial Investment Services and Capital Markets Act ("FSCMA") permits stock repurchase if executed under certain circumstances for the stabilization of management control or stock price (FSCMA, Art 165-2(1)). A stock repurchase can serve as a particularly useful defense strategy when the controlling shareholder lacks the capacity to protect her management control, and it may be preferred by minor shareholders who benefit from the resulting increase in the stock price.[17]

The defense through stock repurchase may be summarized as follows: 1) though treasury shares do not have voting rights, the voting rights can be revived if the shares are sold to friendly third parties; 2) the repurchase of stocks can raise the price of shares by decreasing their number in the market,

13) Unitrin, Inc. v. American General Corp., 651 A.2d. 1361 (Del. 1995).
14) Dale A. Oesterle, supra note 3, at 263.
15) Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.3d. 173 (Del. 1986).
16) Paramount Communications Inc. v. QVC Network, Inc., 637 A.2d. 34 (Del. 1994).
17) Hwa-Jin Kim, *supra* note 3, at 45.

and thereby increase the cost and risk for the acquiring company and reduce its potential gains from the acquisition; 3) because a stock repurchase would reduce the cash held by the target company, the target company will appear less attractive if the aggressor company's aim is to acquire the target company's liquid assets; 4) although the repurchase of shares would not increase the number of voting rights held by the company due to limitations on the number of voting rights that can be acquired through stock repurchase, the proportion of the company's voting rights will increase and thereby allow the company to indirectly defend the management control and; 5) as other kinds of defense strategies are more limited in their effectiveness, it is relatively more advantageous to use stock repurchase for defense of management control.[18)]

2. Discourse on Defense through Issuance of New Shares

Although the target company's defense through the sale of treasury shares is different from defense through the issuance of new shares, these two defense strategies share structural similarities. A defense through issuance of new shares may be regulated under Article 418(2) of the Commercial Act which requires any issuance of new shares to have business purposes. Article 424 which allows shareholders to demand the company to stop any issuance in violation of laws, regulations or its articles of incorporation or in an obviously unfair manner by which shareholders may suffer disadvantages. Citing the above provision of the Commercial Act, the Court has decided in one case that even if the principle purpose of issuing new shares was to defend the current management and there was no sufficient basis for the need to quickly supply funds, the issuance of new shares may be interpreted as having an business purpose under Article 418(2) of the Commercial Act if it can be recognized that maintaining the current management and the controlling shareholder would serve the interest of the company and ordinary shareholder. In determining whether maintaining the current management and the controlling shareholder serves the interest of the company and the ordinary shareholder, the court took into consideration: (1) the purpose of the

18) *Id*.

hostile takeover attempt and the source of the hostile company's funds, (2) operational strategies of the current management and the controlling shareholder, (3) the corporate culture of the target company, (4) the social and economic importance of the target company's business, and (5) the prospect on the continuation of the target company's current business.[19]

3. *Sale of Treasury Shares*

The sale of treasury shares is distinguishable from the issue of new shares in several different ways. First, unlike the issuance of new shares, which is effected mainly to supply capital to the company, the sale of treasury shares, which the company acquired with various objectives including the increase of stock price, stability in management, payment of debt, and supply of security interest, is not undertaken for the primary purpose of capital increase. Second, while Article 418 of the Commercial Act regulates the preemptive right of new shares, there is no provision in the Commercial Act regulating the purchase right of treasury shares. Third, while the issuance of new shares increases the number of total issued shares, the sale of treasury shares does not change the number of total issued shares. Lastly, when new shares are issued to existing shareholders, they do not change the ratio of shareholding, but when they are issued to a third party, they may change the existing shareholders' ratio of shareholding. On the other hand, when treasury shares are sold to specific shareholders or a third party, the existing shareholders' ratio of shareholding may be affected significantly as voting rights that have been suspended are restored. Because of such characteristics of treasury shares, a target company must take into account the particularities of the sale of treasury shares.

4. *Case Precedents on Sale of Treasury Shares*

More recent cases involving the legality of the sale of treasury shares as a defense against hostile takeover include the following: 1) the decision for injunction against the exercise of the Seoul Western District Court on March 24, 2006 (2006*kahap*393); 2) the decision by the Seoul Western Court on June 29,

19) 2003KaHap369 (Suwon District Court Yeoju Branch, Dec. 12, 2003).

2006, confirming that the over-the-counter sale of treasury shares was null and void (2005*gahap*8262) (the "*Daerim Tongsan*g Case"); and 3) the decision by the Suwon District Court on January 30, 2007 (2007*kahap*30) (the "*Fine-digital* Case").

1) Cases Holding the Sale of Treasury Shares Illegal

The Court summarized the *Daerim Tongsang* case as follows: Neither the Commercial Act nor Securities Act(before the enactment of FSCMA) apply regulations for the issuance of new shares to the sale of treasury shares, and the effect of sale of treasury shares is in principle different from that of the issue of new shares because the former action changes neither the total asset of the company nor the existing shareholders' ratio of shareholding. However, the sale of treasury shares can have the same effect as the issue of new shares if the treasury shares are sold only to specific shareholders and the other shareholders' ratio of shareholding is consequently diminished. The sale of treasury shares should, therefore, be regulated like the issue of new shares, and the sale of treasury shares should be prohibited if it is used to avoid regulations. In Daerim Tongsang, the sale of treasury shares had a significant effect on the interest of the plaintiff who was a major shareholder and on the control of the company. Taking into account the motive for the execution of the share purchase agreement and the interests of the parties involved, this Court hold the sale of treasury shares null and void.

This decision is significant in that the Court deviated from case precedents by holding that the sale of treasury shares to specific shareholders violated the rights of other existing shareholders and was thus invalid. The reasons for holding the sale invalid was that: (1) the sale of treasury shares had significant effect on the interest of the existing shareholders and on the control of the company; (2) the other shareholders were not given the opportunity to buy the treasury shares; (3) the treasury shares were sold only to specific shareholders; and (4) taking into account the motive for the execution of the share purchase agreement and the interests of the parties involved, the Court could not overlook the sale. A target company's defense tactics have been supported with the logic that a stock repurchase would have a deterring effect as it increases the cost of hostile takeover. Also, it is argued that if a hostile takeover attempt is already being made, the sale of treasury shares to the controlling shareholder or a friendly third party would increase the number of

friendly shares and thereby help defend the management control. However, with the above decision, it is possible that the sale of treasury shares to the controlling shareholder or a friendly party during a hostile takeover attempt will be held valid only if it was done in compliance with all applicable laws and regulations. Therefore, to use defense measures involving the purchase and sale of the target company's own shares, it is necessary for the target company to take greater caution to comply with all applicable laws and regulations.

2) Cases Holding the Sale of Treasury Shares Legal

In the case of *Fine Digital*, the sale of treasury shares was held legal. The holding of *Fine Digital* is as follows: (1) selling treasury shares is distinguishable from issuing new shares because the former neither affect the company's total assets nor the proportion the existing shareholders' voting rights; if these factors are considered, it is difficult to accept the claim for cancellation of sale of treasury shares, which is similar to a claim for cancellation of issuance of new shares; (2) because the sale of treasury shares involves a third party, the sale can be found invalid only when the third party knew or could have known that the purpose of the sale was to defend the management control; (3) even in situations where the sale of treasury shares can be made void due to the absence of resolution by the board of directors, the sale of treasury shares can be found invalid only if the third party either knew or could have known that the board resolution was never adopted.

The holding in this case outlined above is significant in two aspects. (1) This case was decided on the premise that even if the treasury shares were sold in order to defend the management control, because such sale essentially is selling of shares that have already been issued, there is no effect on the company's total assets or on the proportion of existing shareholders' voting rights. Therefore, in this case, it is difficult to apply the reasoning for holding the issuance of new shares invalid. This case is significant in that it decided that the sale of treasury shares cannot be held invalid only because it was undertaken for the purpose of defending the management control.[20] (2) With

20) For commentary on this decision, see Il-Bong Moon, *Preliminary Disposition Relating to the Sale of Treasury Shares*, 23 BUSINESS, FINANCE & LAW 89 (May 2007).

regard to the legality of a sale of treasury shares that requires the board of directors' resolution, this case was decided on the basis that even if the sale of treasury shares is deemed invalid due to procedural errors on the part of the seller, the sale can be voided only when the other party in the dealing knew or could have known that the seller did not have the board approval. This holding seems to reflect the rule that the company does not assume liability when the other party is unaware of the fact that there was no board resolution when such resolution is required.[21] However, it can be inferred from this case that if the sale of treasury shares is for defending the management control and if the directors acted out of malice for the benefit of a major shareholder or for an illegal benefit of a director, thereby violating the public order and morals, such sale of treasury shares can be voided.[22]

5. Legality of the Sale of Treasury Shares to a Third Party

There is no standard prescribed in FSCMA, the Commercial Act or related regulations for determining whether the sale of treasury shares to a third party during a hostile takeover attempt is legal. Because of the lack of standard, it appears that, in the past, such sale of treasury shares was deemed either legal or subject to the business decision of the directors. More recently, however, attempts are being made to apply Article 418 of the Commercial Act, dealing with preemptive right of new shares, or Article 424 of the same Act, dealing with issuance of new shares, to the sale of treasury shares discussed above, and the *Daerim Tongsang* case was an example of such attempts.

Unlike in Japan where regulations for the issuance of new shares are applied to the sale of treasury shares, it appears that in Korea it would be difficult to apply Articles 418 and 424 of the Commercial Act to a situation where new shares are not being issued. This is because whereas an issuance of new shares accompanies a capital increase, any increase from the sale of treasury shares may be deemed as the return of capital of capital to its original place. While the Commercial Act and FSCMA and the related regulations

21) *See e.g.*, 97Da34709 (Supreme Ct., Mar. 27, 1998).
22) Il-Bong Moon, *supra* note 21, at 100.

prescribe rules for the purchase of the company's own shares, the two Laws do not contain any provision on the sale of treasury shares, aside from some procedural rules in FSCMA relating to regulatory reporting. As the sale of treasury shares is considered a profit and loss transaction to which the principle of shareholder equality does not apply, and as such sale is a personal transaction between the transacting parties, any limitation on such transaction should be carefully considered. Moreover, the application of regulations for the issuance of new shares may result in diminished benefits of financial management due to strict procedural requirements.[23] Therefore, it would be most reasonable to view the board of directors as having the authority to decide on the sale of treasury shares, whether such transaction takes place on exchange or over the counter, and whether the treasury shares are sold to existing shareholders or to a third party. In principle, if the board of directors decides to sell legitimately acquired treasury shares in compliance with relevant laws and regulation, the resulting sale should be treated as legal. The holding in *Fine Digital* discussed previously seems to be based on this principle. Those who view the repurchase of the company's own shares as a legitimate defense against a hostile takeover attempt presuppose that the sale of legitimately acquired treasury stocks to existing shareholders or a third party is also a legitimate transaction. Even if treasury shares are sold to defend the management from a hostile takeover attempt, it would be most appropriate to determine the legality of such sale by examining whether the defense was reasonable under the given circumstance.[24]

If the board of directors has the authority to make a business decision on the sale of treasury shares, then the legality of the decision should be determined by applying the principle of business judgment, which is the standard applied for evaluating board actions. In evaluating the legality of the board decision, a determination on whether the treasury shares were initially acquired by the company in compliance with relevant laws and regulations would be an important step. Furthermore, the decision of the board can be evaluated using the 'principle of reasonable basis' and the 'principle of

23) Jong Joon Song, *A Study on Regulating the Procedures in the Sale of Treasury Shares*, 3504 THE LAW TIMES (Nov. 8, 2006).

24) *Id.*

proportionality' discussed above. The directors can be protected under the principle of business judgment if there was reasonable basis for the belief that the hostile takeover attempt posed a risk to the company policy and the defensive measure taken was reasonable in relation to the degree of the threat posed against the company. However, if the sale of treasury shares is only for the interest of the controlling shareholder rather than for the interests of the company and its shareholders who are faced with a hostile takeover attempt, the decision of the board to sell treasury shares may be held illegal.

The sale of treasury shares to specific major shareholders per se may not violate the principle of shareholder equality. Nonetheless, it may be a violation of the principle of equality as well as the directors' duty of care as fiduciaries if the company sells the treasury shares to specific shareholders for a price that is significantly lower than the market price.[25)] Even under such circumstance, the determination on the reasonableness of the sale should be based on various factors including the reasonableness of the purchase price, the source of the purchase money, the cause of contest over management control, the long-term development plan of the company, how the hostile party came to acquire shares, and the major shareholders' long-term interests.

Determining the reasonableness of the purchase price should not be difficult if the shares of the company are listed on the Korea Stock Exchange or KOSDAQ and a market price is established. However, if the company shares are not listed and a market price is unavailable, determination of the reasonableness of the purchase price may require complex procedures. The 'market price' of an unlisted share can be determined using the following principles: (1) if there exists an objective exchange value that is established through a transaction conducted in a normal and ordinary manner, that objective exchange value should be the market price;[26)] (2) even if there is no such other transaction, if the purchase price can be deemed objective because

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25) In the U.S., there are case laws holding that it is a breach of fiduciary duty for directors to sell the company shares to a specific group of shareholders at a price below the best price for those shareholders to gain control over management without giving the same opportunity to the other shareholder. *See* e.g., Schwartz v. Marien, 43 App Div 2d 307, 351 NYS 2d 216.

26) 86Nu318 (Supreme Ct., Jan. 20, 1987); 86Nu408 (Supreme Ct., May 26, 1987); 88Nu4997 (Supreme Ct., Mar. 27, 1990); 90Nu4761 (Supreme Ct., Sep. 28, 1990); 92Nu1971 (Supreme Ct., Oct. 27, 1992).

the purchase was conducted in a normal and ordinary manner, then the purchase price may be treated as the market price;[27] (3) if there exists no other transaction and if the purchase price cannot be treated as the market price, then the appraised value pursuant to the Inheritance Tax and Gift Tax Act shall be deemed the market price. If the company sells its shares at a price that is substantially lower than the market price, the sale of the shares may be held invalid, and the directors who approved the sale may be held liable both criminally and for damages. If the directors are shown to have placed their own interest ahead of the interest of the company, they may be held responsible for breach of the duty of loyalty.

6. The White Knight Strategy and the Sale of Treasury Shares

The white knight strategy refers to a passive defense tactic in which the target company finds a third party purchaser who would buy the company under the condition that is more favorable to the current management of the target company. There is also what is called the white squire strategy in which the target company finds a third party purchaser who would buy only a minority of shares without gaining management control and take a position that is favorable to the current management. In Korea, the white squire strategy is understood to be a type of white knight strategy.[28]

It appears that the use of the white squire strategy can be quite helpful. In addition to helping the company defend against a hostile takeover attempt, the white squire strategy can improve the financial condition of the company with the sale of treasury shares, and the funds acquired from the sale enables the company to repurchase its own shares in the future. If the white squire strategy is adopted, the legality of such strategy would be determined based on whether the treasury shares were sold at a reasonable price to an appropriate third party in a reasonable manner.

While the white squire strategy can be used as a defense strategy against a hostile takeover attempt that is already taking place, it may be more effective

27) 86Nu408 (Supreme Ct., May 26, 1987); 92Nu1971 (Supreme Ct., Oct. 27, 1992); 93Nu22333 (Supreme Ct., Dec. 22, 1994); 2001Du5903 (Supreme Ct., May 27, 2003).

28) Jae-Yeol Kwon, *supra* note 2, at 140.

as a preventive measure against a potential hostile attack. For example, financial plans that involve the transfer of treasury shares, such the issuance of exchangeable bonds and convertible bonds, may help prevent hostile takeover attempts. However, because it is possible for a white squire to betray the management and try to takeover the company, the company must use a trustworthy party as the white squire, cause the white squire to enter into a stand still agreement for mutual nonaggression,[29] employ cross ownership of shares to the extent the voting rights are not limited due to mutual ownership,[30] or employ a strategic cooperation arrangement that can hold each other in check.

KEY WORDS: takeover, stock repurchase, director's duties, treasury shares

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29) When using the white squire strategy, the company offers additional shares to the white squire with the condition that the white squire would enter into a stand still agreement requiring the white squire to side with the current management in the face of hostile takeover attempt. ARTHUR R. PINTO, UNDERSTANDING CORPORATE LAW, § 12.04.

30) In recent years, the Korean press has been reporting more frequently about the use of cross ownership as a defense strategy against a hostile takeover attempt. For example, Maeil Business Newspaper published an editorial on July 4, 2007 that described the cross ownership of shares between KT&G and Shinhan Holdings as a type of white knight strategy employed to defend the management control. The editorial praised the cross ownership of shares as the best defense strategy that is permitted by law.