

April 8, 1976

To Our Clients:

Going Private - Second Step Acquisition Freezeouts

In Merrit v. Libby, McNeil & Libby, (2d Cir., No. 76-7136, Apr. 5, 1976), a second-step short-form cash merger following a cash tender offer, involving the same facts as Tanzer Economic Associates, Inc. v. Universal Food Specialties, Inc., described in our Memorandum of March 15, 1976, the Second Circuit narrowed the scope of its holdings in Marshel v. AFW Fabric Corp. and Green v. Santa Fe Industries, Inc.

Green was distinguished on the ground that it involved a motion to dismiss the complaint and presumably therefore the decision was based on the allegation that the second-step short-form merger there involved was at an unfair price and without any business purpose.

Marshel was distinguished on the ground that it involved a shell company formed for the purpose of freezing out the minority, the use of corporate funds for the freezeout, no motive other than the freezeout and the insiders taking advantage of going public at a high price and then going private at a low price.

Merrit was distinguished on the basis that "we do not have the stark situation where the defendants clearly have chosen to force the elimination of the minority by the use of corporate funds solely for their personal advantage and for no business purpose. Indeed, the appellees plausibly assert that their primary purpose was to benefit the corporations, including, [the acquired company], by the merger."

In addition to its apparent acceptance of the second-step freezeout to complete an acquisition as a valid transaction that does not violate Rule 10b-5, the court indicated that where a freezeout transaction does violate the federal securities law the measure of damages is not that available under state appraisal statutes, but might embrace the Brudney and Clurelstein "fair shares" concept.

While Merrit is only a procedural holding on the preliminary injunction issue, it is an important indication of an attitude not to embrace an all pervasive per se prescription of freezeouts and to accept the natural concomitants of such transactions (elimination of conflicts and reduction of overhead) as the requisite motivation.

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