WACHTELL, LIPTON, ROSEN & KATZ

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To Our Clients:

Going Private; Long-Form Freezeout Merger; Second Step Acquisitions.

Despite recent cases in other jurisdictions to the contrary, Delaware has reiterated its position that absent fraud or blatant overreaching a long-form cash merger may be used to freezeout the minority shareholders of a subsidiary even though the freezeout does not serve any corporate or business purpose of the subsidiary and the minority has no voice in determining whether the merger will be effected. A minority shareholder freezeout is a proper use of the Delaware merger statutes -- both short form and long form -- and the sole remedy of the minority is an appraisal proceeding. Singer v. Magnavox Co., Civ. No. 4929 (Del. Ch., Oct. 26, 1976).

North American Philips Corp. (NAPC) made a hostile cash tender for all the shares of Magnavox at $8 per share at a time when the market was substantially less than $8. Magnavox opposed the NAPC tender on the ground that the price was inadequate in light of the $11 per share book value of Magnavox. After the usual skirmishing, management of Magnavox reached an accommodation (two-year employment contracts at their then salaries) with NAPC which resulted in an increase in the tender price to $9 per share and withdrawal of opposition to the tender. The tender offer stated NAPC's purpose to acquire the entire equity of Magnavox and intent to acquire any shares outstanding after the tender by merger or other means. The tender drew 84% of the Magnavox shares and NAPC took full control of Magnavox. A few months later NAPC caused Magnavox to enter into a long-form cash merger agreement at $9 per share. No corporate or business reason for the merger was advanced other than the desire of NAPC to eliminate the minority and achieve full ownership of Magnavox. The merger was submitted to a vote of the Magnavox shareholders at a special meeting. Since NAPC owned 84% of the shares and did not agree to vote in accordance with the vote of the minority, the minority vote was meaningless and, as a practical matter, the merger was effected by the action of NAPC.

Relying on David J. Greene & Co. v. Schenley Ind. Inc., 281 A.2d 30 (Del. Ch. 1971) the court summarized the Delaware law with respect to freezeout mergers as "(1) unless a minority shareholder could show fraud or blatant overreaching on the part of the majority in eliminating his stock interest through merger, the merger itself, and the reasons for it, were not subject to attack, and (2) a merger designed primarily to eliminate minority shareholders was not an improper use of either [the long-form or short-form merger provisions of the Delaware Corporation Law]."

The court rejected the recent federal and state cases (E.g., Green v. Santa Fe Ind. Inc., 533 F.2d 1283, rehearing denied 533 F.2d 1309 (2d Cir. 1976); Berkowitz v. Power/Mate Corp., 342 A.2d 567 (N.J. Super. 1975); Jutkowitz v. Bourns, Civ. No. 000268 (Cal. Super. Nov. 19, 1975)) that have invalidated freezeouts that were not justified by a business or corporate purpose of the subsidiary. The primary basis for rejection was the basic Delaware doctrine that a corporate transaction that is authorized by the Delaware Corporation Law is viewed as an independent transaction that does not need any extra-statutory justification -- motive is not significant if the transaction is specifically authorized by statute. In addition, the court noted that Power/Mate and Bourns involved going public high and going private low and said:

> "Admittedly there seems something fundamentally inquitable about such a stark progression of events and perhaps a use of the Delaware statutes should not be permitted which would allow those with controlling interests who originally sought public participation to later kick out public investors for the sole reason that they have outlived their utility to those in control and are made easy pickings by existing market conditions. However, if such an exception is to be made it must wait for another day because, according to the complaint, such a situation does not exist here."

The court also held that various allegations of fraud and breach of fiduciary duty by NAPC and the directors of Magnavox in effecting the merger amounted to no more than a complaint as to fairness of the merger price as to which appraisal was the exclusive remedy and that even where there are proxy statement disclosure violations, the Delaware counterpart of Rule 10b-5 is not violated when a majority stockholder effects a merger as to which the minority has no voice because the merger was accomplished by the action of the majority and not "by or through the use of" the deficient proxy statement.

M. Lipton