

July 11, 1977

To Our Clients:

State Takeover Laws

The decision by the Ohio Commissioner of Securities in Matter of Esmark, Inc. is another instance of interpretation of the state takeover laws to avoid undue interference with tender offers, confirming the experience to date that these laws are being applied so as to provide 60 to 90 days delay but not to make it impossible to make a hostile tender offer.

The Ohio law has a provision that if a raider acquires more than 5% of a target, the raider may not make a tender offer for 12 months after the last purchase unless prior to going over 5% the raider announced publicly its intention to gain control of the target. In Esmark this provision was held to apply only if the raider had a firm intention to seek control at the time it went over 5%. The factors considered to be determinative were:

1. No consultation with an investment banker prior to 5% purchase.
2. The initial purchase of more than 5% was in response to an unsolicited offer.
3. Outside counsel was not consulted prior to the purchase.
4. No Board of Directors action prior to the initial purchase.
5. No contact with management of the target prior to the initial purchase.

The Esmark decision also contains language condemning "creeping" tender offers. The decision indicates that after reaching a determination to make a tender offer subsequent open market purchases are a "creeping" tender offer and that mere passage of time between the last open market purchase and the announcement of the tender offer does not assure that the purchases were not a "creeping" tender offer.

Fairness Opinions

The Supreme Court decision in E.I. duPont deNemours & Co. v. Collins, rejects the argument that in a conflict merger the controlling company must concede terms at least as favorable as might be exacted in arms-length bargaining

between strangers and sustains such a merger upon a finding of economic fairness to the controlled company. The policy and conceptual framework of the duPont decision is contrary to the rationale underlying the Brudney and Chirelstein "fair shares" argument and duPont can be cited as negating the Seventh Circuit's recent acceptance of fair shares in the Mills case.

duPont involves the tax-free merger of Christiana Securities, a closed end investment company owning 28% of duPont, into duPont thereby giving Christiana shareholders direct ownership of duPont shares and eliminating a market discount of about 25% with which Christiana has historically been burdened. The merger terms were based primarily on the net asset value of Christiana. Essentially each share of duPont owned by Christiana was determined to be equal in value to a share of duPont to be issued on the merger. The merger ratio provided a 2.5% haircut in favor of duPont. Because of Christiana's investment company status, the merger was subject to SEC approval. The SEC stressed net asset value as the principal valuation factor in an investment company merger and held that Section 17 of the Investment Company Act mandates fairness to both the investment company and the merger partner it controls. The Eighth Circuit reversed the SEC on the grounds that the SEC did not consider the substantial benefit to Christiana in eliminating the historic 25% market discount through a tax-free merger. The Supreme Court sustained the SEC's reliance on net asset value as the key factor in an investment company merger.

Directors of Delaware Corporations

Immediately following the decision of the Supreme Court in Schaffer v. Heitner holding the Delaware sequestration law unconstitutional, Delaware enacted a statute which makes nonresident directors of a Delaware corporation subject to suit in Delaware in all actions by or on behalf of, or against the corporation.

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