WACHTELL, LIPTON, ROSEN & KATZ

February 2, 1983

To Our Clients:

Takeovers; Lockup Options

The January 27, 1983 decision in the Buffalo Forge case sustains a $26 per share lockup stock option granted in connection with a $32.75 white knight merger agreement. The court said the manipulation theory of the Marathon case was not applicable because the Buffalo Forge option did not stifle the bidding (there were in fact three subsequent bids).

The option (actually a sale of 425,000 shares in exchange for a 10-year 9% note and an option on 143,400 shares) was at the $32.75 merger price; $26 was the present value of the note. In sustaining the option, the court said that it took into account that $26 was more than the book value and the trading price prior to the initial tender offer. The court also laid great emphasis on the fact that the option was a consideration demanded by the white knight as a condition to making its offer.

The Buffalo Forge case also reaffirms the applicability of the business judgment rule to takeovers and holds that an investment banker's engagement on a percentage-of-increase-in-price fee basis does not create a "conflict of interest" on the part of the investment banker.

M. Lipton

83-0011