WACHTELL, LIPTON, ROSEN & KATZ

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To Our Clients:

Takeover Issues for 1987

Mergers, takeovers and LBOs continued at a high rate during 1986 and it appears that they will do the same in 1987. The key issues during 1987 are likely to be:

Tax. The new tax law virtually eliminates NOLs after an acquisition and repeals the General Utilities doctrine. While these changes are not favorable for acquisitions and during the first half of 1987 they may well slow in response, in the long run the tax changes are not likely to reduce significantly acquisition activity.

Financing. Unlimited junk bond financing will continue to be available. The $7 billion highly confident letter Drexel Burnham has furnished for the Icahn bid for USX is a new high, but it will probably be topped in 1987.

Restructuring. The current fad is restructuring. The public LBO of the Owens Corning Fiberglas and FMC types, the publicly offered junk-bond-financed LBOs of the Macy type and the spin-offs of the Dart & Kraft-Premark and Allied-Signal-Henley types will continue. Many of the leading investment banking firms are now participating as major equity partners in LBOs and restructuring transactions and the refrain is "you had better take the initiative and restructure yourself before some raider forces you."

Scaled Voting. The NYSE has now formally proposed its new listing rule abandoning the one-share, one-vote concept. If approved by a majority of the outstanding shares, a listed company can have non-voting common or limited voting common. Although institutional investors will be heavily opposed and shareholder approval hard to obtain, 1987 will see a marked increase in attempts to obtain scaled voting. It is the best -- indeed the only practical -- defense against open-market raids. The voting limitation likely to become the most popular is the provision limiting any one holder to no more than 10% of the vote no matter how many shares held. One way to obtain scaled voting is in connection with a spin-off; the shareholder vote on the spin-off can also amend the parent's charter and the subsidiary can be established with a scaled voting charter.

Shareholder Rights Plans. Well over 300 companies have adopted rights plans in the year since the Delaware Supreme Court decided the Household case. The CTS, NL and Preway cases will not stop the movement. At most, they will eliminate the flip-in provisions contained in some plans and bring home the message that the best time to adopt a plan is before an attack. The SEC continues its opposition to plans and is soliciting comments on a proposal to eliminate the ability of a board of directors to adopt a plan. Such a proposal is beyond the power of the SEC and is not likely to be enacted. Raiders will continue to litigate against plans and the refusal of a target's board to redeem the rights to permit a hostile bid to go forward. The plans have proved to be very effective in curbing abusive takeover tactics and increasing the negotiating strength of the target's board and will continue to be popular in 1987.

State Statutes. The second generation state takeover statutes such as Indiana and Ohio have not fared well in the federal courts. The Supreme Court will decide their fate in 1987. The New York statute that proscribes merger (and thereby restricts greatly bust-up takeovers) for five years after a non-negotiated acquisition of control, does not in any way prevent or restrict tender offers or open-market purchases and should avoid the constitutional problems of the first and second generation statutes. Much will be learned from the new Supreme Court decision.

Pennsylvania and Maine have statutes that permit the directors of a target to take into account constituencies like employees, customers, suppliers and communities, in addition to shareholders, when considering a takeover. The Delaware Supreme Court took a similar position in the Unocal case, but seemed to retreat somewhat in the Revlon case. With the recent confusion as to the scope and operation of the business judgment rule, it would be very helpful if statutes permitting directors to consider constituencies other than shareholders were adopted in Delaware and the other states.

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