

March 22, 1988

To Our Clients

The Poison Pill -- Status Flip-in

In the Federated Department Stores case, in the context of a preliminary injunction motion, the court, applying Delaware law, held valid a poison pill with a 30% status flip-in (which could be reduced to 15% upon a board finding that an acquiring person was adverse). It was within the business judgment of the board of directors to determine that such a pill was appropriate to protect against abusive takeover tactics. The court said the pill "provides the directors with a shield to fend off coercive offers and a gavel to run an auction."

With respect to a second issue -- the use of the pill to favor one offer over another -- the court held that so long as it was being used by the target to obtain what the board reasonably believes to be the best price, the pill could be used to favor one offer. The court left open the question whether when the auction ends, with the bidders having made their final bids, the pill would have to be redeemed so that the shareholders would be free to choose between the competing bids.

I believe the court's holdings to be absolutely correct. Assuming they are not disturbed on appeal, the Federated-type pill will undoubtedly become the norm for Delaware corporations.

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