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To Our Clients:

National Starch Type Acquisition Called Into Question

The Ninth Circuit decision earlier this week in Epstein v. MCA INC. calls into question the well-known form of acquisition that involves a cash tender offer for most of a company's common stock combined with a recapitalization that permits certain shareholders to convert their common stock into preferred stock on a tax-free basis. The agreement for the recapitalization is entered into prior to the tender offer and closed after the tender offer. This form of acquisition is designed to accommodate an older shareholder who does not want to realize a capital gain, but prefers to postpone sale and allow his shares to pass to his estate and receive a stepped-up basis.

In a decision that rejects the widely-held view that SEC Rule 14d-10 applies only during the actual tender offer period, the court held that the Rule's requirement that a tender offer be open to all holders and that every shareholder receive the highest price, is violated by the usual National Starch type transaction.

The SEC did not raise any Rule 14d-10 issues in connection with the transaction when it was effected in 1990. However, in light of the Ninth Circuit decision, the National Starch type transaction is questionable unless and until the law is clarified.

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