

August 31, 2010

Landmark Case Provides a Road Map for Collapse of a Dual-Class Capitalization

The Magna International case (discussed in our August 17 [memo](#)) in Canada, was affirmed on appeal yesterday. It will be a landmark decision on the difficult issue of comparative fairness in change-of-control situations. The essential facts are:

- Magna had a dual-class capitalization:

112,072,348 Class A low-vote shares (one vote)
726,829 Class B high-vote shares (300 votes)

- Prior to the announcement of a proposal to collapse the dual-class structure, the Class A traded on the NYSE at \$62.53. The Class B was held by the founder-chairman of Magna. At the \$62.53 market price the value was:

Class A \$7.008M
Class B \$45M

- The collapse transaction provided for the founder-chairman to exchange the 726,829 shares of Class B for 9,000,000 shares of Class A plus \$300M cash or, at the \$62.53 price of the Class A, a total of \$863M. An 1800% premium.
- As a result of the collapse, the Class B went from 0.6% of the economic value of Magna's equity to 7.4% and from 66.1% of the vote to 7.4%. The Class A suffered an 11.4% dilution.
- The collapse resulted in the Class A market price appreciating from \$62.53 prior to the announcement to \$73.66 on the day prior to the shareholder vote.

The transaction was attacked by institutional shareholders. The investment bank retained by the special committee of directors created by the board to consider the transaction did not give a fairness opinion. (Major investment banks generally do not give "comparative" fairness opinions.) The special committee did not make a recommendation to the shareholders. The premium of 1,800% to the high-vote shares and the dilution of 11.7% to the low-vote shares were each far larger than any Canadian or U.S. precedent transaction. It was expected by the special committee that the announcement of the proposal would be well received by the market with a material increase in the low-vote share price, despite the dilution. A proxy statement for the shareholder meeting called to consider the transaction was approved by the Ontario Securities Commission as satisfying requirements for full disclosure of the facts relevant to the shareholder decision. At the meeting, 75% of the low-vote stock voted to approve the transaction.

The Magna transaction and the Court's decision provide a clear road map for a company's directors, and the investment bankers and lawyers advising them, in a dual-class restructure to create a single class of stock. They also provide interesting facts and analysis that may be of use in other types of change-of-control dual-class transactions.

Martin Lipton