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FORM OVER SUBSTANCE - DELAWARE DECLINES TO APPLY ENTIRE FAIRNESS TO A TENDER OFFER BY MAJORITY STOCKHOLDERS FOR THE MINORITY-HELD SHARES

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In a recent decision, the Delaware Court of Chancery reminds us that when a majority shareholder seeks to eliminate the minority, the form of the transaction rather than its substance will often determine the applicable standard of review of the transaction. In In Re Siliconix Incorporated Shareholders Litigation (C.A. No. 18700, June 19, 2001), the Chancery Court declined to enjoin an exchange offer by Vishay Intertechnology, Inc. ("Vishay") for the 19.6% equity interest in Siliconix Incorporated ("Siliconix") it did not already own, holding that absent coercion or disclosure violations (a) the tender offeror was not under any duty to offer a fair price and (b) the transaction was not subject to the "entire fairness" standard.

The Court acknowledged that the transaction would have received greater scrutiny had the transaction been structured as a merger and seemed perplexed by this difference in treatment, especially since in this case, if the exchange offer was successful and a short-form merger was accomplished, the Siliconix minority shareholders would be in the same position as if the transaction had been structured as a merger, *i.e.*, they would all become Vishay shareholders. Nevertheless, the Court justified the difference in approach as follows:

- Accepting or rejecting a tender offer is a decision to be made by the individual shareholder.
- The target in a merger enters into a merger agreement, but the target company in a tender offer does not have to make such a decision because the target of a tender offer is not the corporation but, rather, its shareholders. Section 251 of the Delaware General Corporation Law ("DGCL") imposes specific duties on the directors of corporations entering into merger agreements but does not impose similar duties on directors of tender offer targets.

Vishay, a manufacturer of electronic and semiconductor components, owned 80.4% of Siliconix, a NASDAQ-listed manufacturer of semiconductor products. On May 25, 2001 Vishay announced an exchange offer under which it would exchange 1.5 shares of Vishay for each Siliconix share. Vishay's offer contained a non-waivable "majority of the minority" condition so that Vishay could not proceed with its tender offer unless a majority of the shareholders not affiliated with Vishay tendered their shares. Vishay also stated that it intended to effect a short-form merger following a successful tender offer, but that there might be circumstances under which it would not do so. On June 8, 2001, Siliconix, which had established a Special Committee, filed a Schedule 14D-9 stating that the Special Committee would remain neutral. The Special Committee did not seek a fairness opinion.

The action was brought by a shareholder of Siliconix seeking a preliminary injunction against Vishay's exchange offer alleging that (1) disclosures to minority stockholders were inadequate, (2) the offer was coercive, (3) the offered price was unfair and, because of disclosure violations and the coercive nature of the offer, defendants could not satisfy their burden of demonstrating the fairness of the price, and (4) the tender offer must be judged by the entire fairness test.

Fair Price Claim. The Court rejected the claim that the tender offeror was under a duty to offer a fair price stating that "as a general principle, [Delaware] law holds that a controlling shareholder extending a tender offer for minority-held shares in the controlled corporation is under no obligation, absent evidence that material information about the offer has been withheld or misrepresented or that the offer is coercive in some significant way, to offer any particular price for the minority-held stock." Here, because the Court concluded that there were no disclosure violations and the tender was not coercive, Vishay was not obligated to offer a fair price in its tender.

Entire Fairness Standard. In response to plaintiff's claim that the fair dealing and fair price prongs of the entire fairness standard were implicated because the Siliconix directors breached their duties of care and loyalty, the Court stated that, unless coercion or disclosure violations can be shown, no defendant has the duty to demonstrate the entire fairness of the proposed tender offer.

Plaintiff maintained that the Siliconix board was required by McMullin v. Beran, 765 A2d 910 (Del. Sup. 2000), to take a position on whether the Siliconix shareholders should accept the tender and to inform them of the reasons for it. In McMullin, ARCO owned 80.1% of the stock of ARCO Chemical. It sought the sale of all of Chemical through a merger of Chemical into a subsidiary of Lyondell. McMullin holds that in the context of the merger of a subsidiary with a third party where the controlling shareholder wants the merger to occur and the minority shareholders are powerless to prevent it:

- the directors of the subsidiary have a duty to protect the minority shareholders' interests;
- the board cannot abdicate its duty by leaving it to the shareholders alone to determine how to respond; and
- the board has a duty to assist the minority shareholders by ascertaining the subsidiary's value as a going concern so that the shareholders may be better able to determine whether to seek appraisal rights.

In both the McMullin and Siliconix transactions, the decision of the minority shareholders was either (a) to take the consideration offered or (b) to seek appraisal. However, in McMullin the duties imposed on the target's directors were statutory duties imposed by § 251 of the DGCL (relating to long-form mergers) and the "attendant" fiduciary duties. The Court declined to extend the duties imposed by McMullin to the conduct of the directors of a tender target.

The court pointed out, as an additional justification for the distinction between McMullin and the Siliconix situation that the minority shareholders in McMullin were powerless because the parent was voting for the merger and it did not matter how they voted, but the Siliconix minority shareholders had the power to thwart the tender offer because it would go forward only if a majority of the minority shares were tendered. The Court declined to enjoin the offer, mentioning its "reluctance…to deprive the

Siliconix shareholders of the opportunity to exchange their shares or of the opportunity to exercise their majority will to derail the tender under the 'majority of the minority' tender aspect of the proposed transaction." The latter is exactly what happened on July 5, 2001 when the exchange offer expired without any shares being purchased because the "majority of the minority" condition was not satisfied.

As the case was decided on the comparison between the statutory duties of directors under §251 of the DGCL and the lack of such duties in a tender offer situation, it is not clear whether the "majority of the minority" self-imposed condition was really required as a legal matter. Future cases may sort that out.

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This memorandum constitutes only a general description of the Siliconix decision and should not be construed as legal advice.

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