

Dear clients and friends,

Determining the Fair Value of a Company in the Context of a Full Tender Offer

January 2010

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The Supreme Court of Israel recently delivered a precedent ruling, in which it determined that the preferred method for assessing the fair value of a company, in the context of a motion for an “appraisal remedy” following a full tender offer, is the **Discounted Cash Flow (“DCF”)** method (CA 10406/06 Dan Atzmon v. Bank Hapoalim Ltd. (published in *Nevo*, ruling handed on December 28, 2009).

Under the Israeli Companies Law, 1999 (the “**Companies Law**”), a person may not acquire shares of a public company that would result in such person holding more than 90% of such company’s issued and outstanding share capital, other than by offering to purchase the shares of all shareholders of such company by launching a “full tender offer”. If the rate of non-acceptance of such a full tender offer is under 5% of the issued and outstanding share capital of the company, the offeror may force the dissenting shareholders to sell their shares for the price stipulated in the full tender offer.

In order to provide the minority shareholders with some protection, the Companies Law enables shareholders to file a motion to court seeking an “appraisal remedy”, *i.e.*, arguing that the price paid for the shares in the full tender offer was below their fair value.

The respondent in the case at hand, Bank Hapoalim, completed a successful tender offer for the purchase of all shares of a publicly traded Israeli company. The appellant, Atzmon, filed a motion for an “appraisal remedy”, arguing that the price paid by Bank Hapoalim for such shares was below their fair value.

The Supreme Court concerned itself with the method that should be used for assessing a company's fair value in the context of a motion for an appraisal remedy.

The Supreme Court ruled that the fair value of a company should be determined using DCF, reflecting a company’s intrinsic value, which is based on parameters deriving directly from the company's going concern value to its shareholders. Such intrinsic value is based, *inter alia*, on the company's existing assets and its present and future income (*i.e.*, both its current capitalized cash flow, and its future capitalized cash flow, derived from future investment opportunities).

The Supreme Court rejected two other methods of assessment:

1. Assessment Based on Market Price: Amongst other reasons for rejecting this method, the Supreme Court explained that it is prone to manipulation by offerors, which are often the controlling shareholders of the company whose share are being purchased. Such offerors may use their position to determine the timing and conditions of the offer in order to dictate unfair conditions.
2. Assessment Based on Asset Value: This method was denied by the Supreme Court since it considered a conservative method which relies on the company's past financial information and does not express the company's full value, as a going concern.

Thus, the Supreme Court determined that the preferred method for assessing the fair value of a company in the context of a motion for an appraisal remedy following a full tender offer is DCF.

Nevertheless, the Supreme Court noted certain circumstances in which the evaluation of a company may be unnecessary. An example of one such circumstance may be when an off-market (private) acquisition is executed in proximity to the full tender offer in question; another is when the company’s shares are widely dispersed and heavily traded.

In Atzmon v. Bank Hapoalim, the Supreme Court ruled against the appellant, determining that the fair value of the company's shares, based on DCF, matched the price offered by Bank Hapoalim in its full tender offer.

We note, that although the Supreme Court’s decision may be limited to the specific context and circumstances of a motion for an appraisal remedy following a full tender offer, the Supreme Court’s preference of DCF may be implemented in other cases that call for assessment of the fair value of companies, and thus may have a lateral effect on company evaluations in Israel.