To Our Clients:

PRIVATE PLACEMENTS

RULE 146

Rule 146 has been adopted with an effective date of June 10, 1974. While there have been several changes from the version of the Rule proposed on October 10, 1973, essentially the Rule as adopted follows the proposed Rule. The adoption of Rule 146 completes the 140 series of rules which reflect implementation by the SEC of a major aspect of the 1969 Wheat Report recommendations. In retrospect the SEC, building on the base of the 1964 amendments making all "public" companies subject to the 1934 Act reporting requirements, has performed an almost unique administrative restructuring and modernization of the federal securities laws and thereby achieved substantial integration of the 1933 and 1934 Acts. Like the other 140 series rules, Rule 146 represents a perceptive balancing of protection of the public with practical convenience and everyday utility; it provides the certainty of availability of the private placement exemption missing since SEC v. Continental Tobacco Co., 463 F.2d 137 (5th Cir. 1972) appeared to adopt the extremely restrictive interpretation urged by the SEC.

In broad outline, Rule 146 assures the availability of the private placement exemption where:

(1) There are no more than 35 purchasers;

(2) Each offeree is either (a) sophisticated or (b) rich and represented by a sophisticated agent who is not affiliated with the issuer and who discloses any conflicts;

(3) Each offeree has access to registration statement-type information (which for reporting companies may consist of the latest Form 10K or equivalent and the subsequent 1934 Act filings together with a description of the transaction) and whatever additional information he requests;

(4) The issuer does not use means of general solicitation or general advertising to reach the offerees; and

(5) Each purchaser signs an investment letter and the issuer legends the securities and places stop transfer orders.

Nonexclusivity and Availability

Rule 146 is not exclusive; it is a safe harbor. A private placement that does not meet all the requirements of Rule 146 may still be exempt under the general interpretation of § 4(2) of the 1933 Act. However, despite the very clear disclaimer of exclusivity by the SEC in the introduction to Rule 146, it is doubtful that the SEC or the courts will be sympathetic to private placements that fail to meet the standards of Rule 146 in a substantial way. The prudent practice will be to follow Rule 146 in all private placements and to go outside Rule 146 only on the advice of counsel.

Rule 146 is available only to issuers. It does not apply to private placements by control stockholders or holders of restricted securities. Such holders may still use private placements (not a "distribution" and therefore no "underwriter" involved), but they do not have the benefit of the Rule 146 safe harbor. Again, as a practical matter, any such private placement should conform to the requirements of Rule 146.

Rule 146 and the general private placement exemption are exemptions only from the registration requirements of the 1933 Act; the fraud provisions of the 1933 and 1934 Acts are fully applicable to all such private placements.

The issuer has the burden of proving the availability of Rule 146 as to each offeree as well as to each purchaser. Careful written documentation as to the sophistication and suitability determinations and the disclosure of information should be maintained by the issuer and any broker or agent acting on behalf of the issuer.

The previously proposed requirement for filing a report with the SEC of each Rule 146 transaction has been abandoned.

Number of Purchasers

Rule 146 limits each private placement ("an offering") to 35 purchasers; purchasers not offerees. Certain purchasers are not included in counting the number of purchasers. Close relatives of a purchaser and trusts and other entities wholly owned by a purchaser and his close relatives do not count. Any person making a cash purchase of $150,000 or more does not count. All of the other provisions of Rule 146 apply to purchasers excluded from the 35 purchasers limitation.

Corporations, partnerships, trusts and other entities are a single purchaser unless formed for the specific purpose of acquiring the securities offered in the Rule 146 transaction, in which case each beneficial owner of the entity would be counted as a separate purchaser.

Each customer of a broker-dealer, each client of an investment adviser, each trust managed by a bank or other trustee and each investment company managed by an investment manager is a separate purchaser for Rule 146 purposes.

Rule 146 provides that any offers or sales, registered or exempt, more than six months before or after a Rule 146 placement will not be integrated with the Rule 146 placement and that any such offers or sales within six months will be treated, for the purpose of determining what is "an offering" within Rule 146, under the traditional SEC integration concepts. If two or more offerings are integrated and the aggregate number of purchasers is more than 35, Rule 146 will not exempt the integrated offerings. Rule 146 states that the following are the factors determining integration: whether (1) the offerings are part of a single plan of financing; (2) the offerings involve the issuance of the same class of security; (3) the offerings are made at or about the same time; (4) the same type of consideration is to be received; and (5) the offerings are made for the same general purpose. Thus, normal bank loans, insurance company debt placements, employee stock plans and acquisitions (other than the continuing-pattern type) can proceed concurrently with each other and a common stock placement to 35 purchasers without any or all running afoul of the 35 purchasers limitation.

Suitability; Kind of Offerees

Rule 146 sets up a double test of suitability--the first before offer; the second before sale.

Prior to making the offer the issuer and any person acting for the issuer must have reasonable grounds to believe and in fact believe that the offeree is either sophisticated or rich. Sophisticated is defined in terms of having such knowledge and experience in business and finance that the offeree is capable of evaluating the

merits and risks of the prospective investment. Rich is defined in terms of ability to bear the economic risk of the investment--holding unregistered securities for an indefinite period and ability to afford a complete loss are indicated by the SEC as appropriate considerations (at least in venture capital placements).

Prior to making the sale the issuer and any person acting for the issuer must make a reasonable inquiry and based thereon have reasonable grounds to believe and in fact believe either that the offeree is sophisticated or that the offeree is rich and together with his "offeree representative" is sophisticated. Thus, an offeree representative can supply the sophistication for the rich but naive offeree.

In order to document the reasonable belief and reasonable inquiry tests, issuers and their agents should adapt the procedures now followed to satisfy the blue sky requirements for private placements in certain states and the SECO suitability rules--obtaining a statement as to financial resources, employment, investment objectives, etc. and an affidavit as to net worth and income.

The offeree representative may be an investment adviser for the offeree, an investment banker or broker retained and paid by the issuer or any other person who meets the Rule 146 test of (1) not being a control person, officer, director, employee or holder of 10% of any class of equity interest in the issuer (except where the offeree is closely related to the offeree representative), (2) being sophisticated, (3) being acknowledged in writing by the offeree as his offeree representative, and (4) having disclosed prior to being designated any material (might be considered important by a reasonable investor in designating a representative) relationship with the issuer or its affiliates which then exists, is mutually contemplated or existed during the past two years and any compensation received or to be received therefrom.

Thus, Rule 146 contemplates the typical brokeer-placed private placement in which the broker is paid by the issuer and places the securities with the broker's customers; the broker in such case being the offeree representative for its customers.

In addition to the nonaffiliation, sophistication, disclosure and acknowledgement requirements for the offeree representative, the offeree representative must (1) act in the interest of the offeree, and (2) be separately designated for each private placement--blanket authorizations to advisers or brokers do not comply with Rule 146.

Furnishing Information; Access

Rule 146 continues the judicial requirement of offeree access to registration statement-type information in terms of a relationship between the offeree and the issuer--employment, family or economic bargaining power.

In addition to registration statement-type information, the issuer is required to:

(1) Afford an opportunity for offeree questions and answer such questions to the extent reasonable;

(2) Permit offeree verification of the registration statement-type information;

(3) Make the same written disclosure to an offeree represented by an offeree representative as the offeree representative is required to make with respect to material relationships between the issuer and the offeree representative; and

(4) Make written disclosure of the risks of ownership and the limitations on resale of restricted securities, including the Rule 146 requirements for legending, stop-transfer order and agreement by the purchaser not to sell absent registration or exemption.

The registration statement-type information may be supplied by a 1934 Act reporting company making available the most recent of its filings on Form 10K, Form 10 or Form S-1 supplemented by any subsequent required 1934 Act filings and a brief description of the securities being offered, the use of proceeds and any material developments not otherwise disclosed. Non-reporting companies must disclose the same information that would be included in a registration statement for the offering except that if audited financials are not available without unreasonable effort or expense, unaudited financials will suffice.

Rule 146 does not make any change in the present practice of using a private placement memorandum that is the substantial equivalent of a 1933 Act registration statement and the usual practices may be expected to continue under Rule 146.

Manner of Offering

Rule 146 does not permit any general solicitation or general advertising. Seminars and meetings, except those limited to qualified offerees and their offeree representatives, are included in proscribed general solicitation.

Limitations on Disposition

Rule 146 requires the issuer to take reasonable care to assure that the purchasers in a private placement do not resell in a manner which would make them underwriters and the placement and resales a distribution. Such reasonable care includes (1) making reasonable inquiry to determine if the purchaser is purchasing for his own account or on behalf of others, (2) placing a legend on the certificates or other documents evidencing the securities indicating that they were not registered and setting forth or referring to the restrictions on transferability and sale, (3) issuing stop transfer instructions to the transfer agent, if any, or making an appropriate notation in the issuer's records if the issuer transfers its own securities, and (4) except for securities issued in business combinations (other than stock-for-stock combinations), obtaining a written agreement from the purchaser that the securities will not be resold without registration or exemption therefrom.

Business Combinations

Rule 146 is available for any transaction of the type required by Rule 145 to be registered under the 1933 Act--essentially "A" mergers and "C" stock-for-assets transactions. "B" stock-for-stock transactions must comply with all of the requirements of Rule 146. The Rule 145-type transactions must comply with all of the provisions of Rule 146 other than the requirement for a signed purchaser agreement not to resell without registration or exemption therefrom and other than that the unsophisticated offeree

be rich as well as represented by a sophisticate. In promulgating Rule 146, the SEC acknowledged but rejected the comments on the previous proposal that the "stubborn widow" can block a Rule 146 business combination. Rule 146 also requires that in business combinations the issuer make special written disclosure of any arrangements with securityholders of the acquired company that are not identical to those relating to all securityholders.

While the "stubborn widow" problem may occassionally block a Rule 146 business combination, essentially Rule 146 allows members of management of the acquired company to act as the offeree representatives for the outside stockholders and thereby accommodates most private placement acquisitions.

Evaluation

Each of the principal types of private placement--institutional debt, bank loan, venture capital, tax shelter, employee stock plan, mom-and-pop start-up, and acquisition of a close corporation--has been reasonably well accommodated by Rule 146. It appears that Rule 146 will fulfil the goal of providing a safe harbor for those transactions which merit the private placement exemption.

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