To Our Clients

Recent Developments

1. Projections. Recently proposed SEC rules (Securities Act Release No. 5581, April 28, 1975, CCH ¶ 80,167) would permit a company that has been a reporting company for three years to include a projection in its 10-Ks and 1933 Act registration statements; require a company that makes projections to file a report on Form 8-K with the SEC within ten days and then periodically thereafter; protect a bad projection against subsequent fraud claims if there was disclosure of the material assumptions and the projection was reasonable and in good faith when made; and permit an independent accountant or other expert to be identified as having reviewed a projection. The SEC release describes the proposals as follows:

> "[T]he proposals are intended to integrate public projections into the disclosure system of the federal securities laws. Proposed rules under both Acts would define a 'projection'. Proposed rules under the Exchange Act would provide for filing a report on Form 8-K under the Exchange Act when a registrant has furnished a projection to any person, with certain exceptions including private financing, preliminary negotiations with underwriters, business combinations and government agencies which have afforded non-public treatment to the projections. A report on Form 8-K would also be required when the registrant has reason to believe that its public projections no longer have a reasonable basis or the registrant has determined to cease disclosing or revising projections . . . ."
>
> "Proposed amendments to Form 10-K under the Exchange Act and Forms S-1, S-7, S-8, S-9 and S-14 under the Securities Act would require the registrant to furnish in the report or registration statement those projections previously filed or required to be filed with the Commission covering year-end results for the registrant's last fiscal year together with comparisons with corresponding historical results. A registration statement would also have to include any projections for the registrant's current and/or next fiscal year if they had been filed. Any registrant that had made projections for its last or current fiscal year or any future period which were filed or required to be filed, would be required to either provide projections for at least six months of the current fiscal year or for the full fiscal year in its report on Form 10-K or explain why it had determined to cease disclosing projections. . . ."

"Proposed amendments to Rules 14a-3 and 14c-3 would require that all projection information contained in the Form 10-K other than exhibits, be included also in the registrant's annual report to security holders. . . ."

"Proposed amendments to Rule 405 under the Securities Act and to Rule 12b-2 under the Exchange Act define a 'projection' to be a statement made by an issuer regarding material future revenues, sales, net income or earnings per share of the issuer, expressed as a specific amount, range of amounts ($1.80 to $2.20) or percentage variation from a specific amount ($2.20 plus or minus 10 percent or 'an increase of 10 percent over last year'), or a confirmation by an issuer of any such statement made by another person. A note has been provided to explain that the definition is not intended to include announcements made to the public regarding preliminary results of period ended but not yet reported. A second note indicates that statements that another person's projection is 'in the ballpark,' 'attainable' or 'on target' are examples of a confirmation."

". . . The projection must have been prepared with reasonable care by qualified personnel and carefully reviewed and approved by management at the appropriate levels and must have a reasonable factual basis and represent management's good faith judgment. . . ."

"As to form, the projection must relate at a minimum to sales or revenues, net income and fully diluted earnings per share; must be expressed as an exact figure, a reasonable variation from an exact figure, or a reasonable range of figures; and must be limited to the registrant's current fiscal year, or if the projection is disclosed after the end of the second quarter, to the current fiscal year and all or any portion of the next fiscal year. . . . [F]or purposes of these rules a ten percent variation or range not exceeding ten percent from the midpoint ($1.80-$2.20) would be deemed reasonable. . . ."

"When disclosed, the projection must be identified as a projection and be accompanied by a statement which (1) discloses the material assumptions underlying the projection, (2) cautions that there can be no assurance that the projection will be achieved since its ultimate achievement is dependent upon the occurrence of the specified assumptions, and (3) indicates that the projection has been prepared on the basis of the specified assumptions and is consistent with the accounting principles expected to be used by the registrant. . . ."

2. Private Placements; Amendments to Rule 146. Securities Act Release No. 5585, May 7, 1975, CCH ¶ 80,168 amends Rule 146 to ameliorate several of the more onerous provisions:

(a) the requirement in 146(c)(3) that any written communication relating to a 146 offering contain an undertaking to provide all of the "access" information about the issuer has been deleted;

(b) nonreporting issuers are now permitted to omit or condense 146(e)(1) financial information that is not material;

(c) 146(f) has been expanded to include an exchange offer as a business combination, along with a merger and a sale of assets for stock; thereby permitting exchange offers without obtaining investment letters and without the unsophisticated offerees having to be rich; and

(d) the 35 purchaser limitation of 146(g)(i) is changed from an absolute limit of 35 to the reasonable belief of the issuer that there are no more than 35.

3. Going Private. The opinion in Green v. Santa Fe Industries, Inc., CCH ¶ 95,085 (S.D.N.Y. 1975) is instructive. Santa Fe owned 95% of Kirby, a Delaware corporation. Santa Fe formed a new Delaware shell and transferred the 95% to the shell. The shell then effected a Delaware short-form merger of Kirby paying the minority $150 cash per share. The next day the minority shareholders were sent a comprehensive information statement detailing the short-form merger and the related Delaware appraisal procedures, a statement of Kirby's income, appraisals of the value of Kirby's stock and assets and a history of the dealings between Santa Fe and Kirby. A Morgan Stanley appraisal of $125 per share based on audited financials for the last fiscal year, unaudited financials for the most recent stub period, Kirby's five-year profit forecast and appraisals of Kirby's assets was appended to the information statement along with the opinions of the asset appraisers. The Court held:

(a) Rule 10b-5 does not supersede state short-form merger statutes; Rule 10b-5 does not proscribe all freeze outs; Rule 10b-5 does not require that there be a valid business purpose--other than elimination of the minority--for a short-form merger.

(b) Rule 10b-5 does not require notice of a short-form merger before it is consummated.

(c) "This Court does not regard Rule 10b-5 as an omnibus federal corporation law having such broad reach as to modify the notice requirements of the Delaware merger statute, or prevent Delaware, in its legislative wisdom from providing a means by which a majority can exclude a minority from the corporation's future affairs, so long as due process is satisfied, as it is here, by the appraisal procedures."

(d) The investment banking opinion, appraisals and history of prior purchases of Kirby stock by Santa Fe satisifed the disclosure requirements, accordingly adequacy of fairness of the merger terms are not at issue under Rule 10b-5.

(e) The proposal of the SEC to adopt specific going private rules under § 13(e) supports the proposition that if full and fair disclosure is made, transactions eliminating minority interests are beyond the purview of Rule 10b-5.

4. Definition of "Security"; Limited Partners and Subordinated Lenders. NYSE v. Sloan, CCH ¶ 95,083 (S.D.N.Y. 1975) holds that limited partners of, and subordinated lenders to, a brokerage firm are "investors" and therefore purchasers of "securities". General partners are not purchasers of "securities".

M. Lipton