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Corporate Securities

A bulletin designed to keep corporate executive and investment banking professionals informed on major developments in the securities industry

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SEC PUBLISHES YEAR 2000 DISCLOSURE GUIDELINES

The SEC has issued an interpretive release setting forth guidelines for public company disclosure of Year 2000 issues. The guidelines were effective August 4, 1998, and apply to companies with June 30 or July 31 fiscal year ends and all companies with quarter ends after the effective date. Companies with quarters ending June 30 or July 31 are encouraged by the SEC to follow the guidelines.

The SEC release focuses primarily on Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") in registration statements and periodic reports. The release provides that Year 2000 disclosure is required if:

- A company has not completed its assessment of Year 2000 issues, *or*
- Year 2000 issues would have a material effect on the company, *without regard to the company's Year 2000 readiness or compliance efforts.*

Under the first prong of the test, a company must assess third-party relationships for Year 2000 effects. Suppliers, vendors, and major customers are to be analyzed for possible impact.

Nearly all companies are expected to have material Year 2000 disclosures under this test.

Adequate disclosure of Year 2000 issues should address:

- *The company's state of readiness* (covering both information and non-information technology systems, the state of readiness of such systems, and the impact of third party relationships and/or risks)

  Costs of Year 2000 compliance (including historical and estimated costs for modifying software and hiring Year 2000 solution providers and the replacement costs of noncompliant systems)

  Risks posed by Year 2000 issues (including description of worst-case Year 2000 scenario)

  Existence of contingency plans (how the company is planning to handle the worst-case scenario)

The statutory safe harbors for forward-looking statements apply to Year 2000 disclosures for eligible companies, particularly projections of capital expenditures, estimated costs of remediation or testing, potential business disruption, and contingency plans. Statements of historical fact regarding actual costs or expenditures, existence of contingency plans, etc., are not covered by the safe harbors.

Possible disclosure can address personnel issues, potential litigation or supervisory or enforcement actions, sources of funds for expenditures, or use of independent verification processes. Tables and charts can be used to demonstrate progress or expenditures to date.

The SEC guidelines also address a number of accounting and financial statement disclosure topics. These topics include the costs of modifying software or being noncompliant, disclosure of Year 2000 commitments or contract defaults tied to Year 2000 readiness, timing of revenue and loss recognition for product upgrades or returns, and write-downs of capitalized software.

Besides MD&A, it may be appropriate to disclose Year 2000 issues in other parts of a registration statement or periodic report. Year 2000 issues may have a bearing on business descriptions, risk factors, legal proceedings, and material contracts (including exhibits). Form 8-K filings may also be appropriate in some cases, especially for companies with effective shelf or short-form registration statements.

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SEC ADDRESSES EURO CONVERSION DISCLOSURE CONCERNS

On July 22, 1998, the staff of the SEC issued its views on the disclosure obligations of public companies in connection with the January 1, 1999 conversion by members of the European Union to a common currency.

Participating countries in the "euro" conversion are Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain. Nonparticipating members that may convert at later dates are Denmark, Greece, the United Kingdom, and Sweden.

The staff is prompting companies to evaluate the impact the euro conversion will have on their businesses. Companies are expected to assess the effect of the different euro conversion stages. The stages include the period before January 1, 1999, the transition period from January 1, 1999 until January 1, 2002 (over which time both the euro and the legacy countries' currencies may be used), the period after January 1, 2002 (when the euro will be the only legal tender), and when a nonparticipating member converts to the euro. Companies are also to consider the impact of the euro conversion on reportable industry segments and each significant line of business.

Euro conversion issues should be disclosed if they are material to a company's business or financial condition regardless of a company's efforts to avoid adverse consequences. If a company is uncertain as to the impact, that uncertainty should be disclosed. Internal analyses or plans for the conversion, or the lack thereof, should be disclosed.

The staff has identified a number of factors to be considered when evaluating the impact of the euro conversion. These include:

- *Competitive Impact* (effect of cross-border price transparency, customer euro pricing requirements, changes in marketing or operating strategies, and single monetary policy on significant markets)
- *Information technology and other systems* (effect of modification of information systems software and fixed assets by issuers, customers, suppliers, banks, and others)
- *Currency risk* (currency exchange costs and rate exposure)
- *Derivatives and other financial instruments* (need for modifying the terms of certain derivatives and other financial instruments, day count and settlement conventions, and risk monitoring systems)
- *Continuity of contract* (application of adopted regulations for continuity of contracts by European Union and various states and ISDA EMU Protocol)
- *Taxation* (effect of IRS rules on euro conversion issues)
- *Accounting* (FASB staff guidance on upgrading or replacing software and fixed assets)

Registration statements and periodic reports are expected to address euro conversion issues, as appropriate, in MD&A, business descriptions, market risk disclosure, legal proceedings, material contracts (including exhibit filings), and risk factors. Form 8-K filings may also be appropriate under specific circumstances.

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PLAIN ENGLISH RULES EFFECTIVE OCTOBER 1

SEC rules for plain English drafting of registration statements take effect October 1, 1998. All registration

statements, supplements to effective shelf registration statements, and post-effective amendments filed on or after October 1 must meet the new requirements.

In August 1998, the SEC issued its final plain English handbook to guide companies under the new rules.

The plain English rules require prospectuses to be clear, concise, and understandable. Companies must write and design the cover pages, summary, and risk factors sections of their prospectuses in plain English.

Six basic writing principles now govern the drafting of the front part of prospectuses. These are:

- Short sentences;
- Definite, concrete, everyday language;
- Active voice;
- Tabular presentation or bullet lists for complex material;
- No legalese or highly technical business terms; and
- No multiple negatives.

In addition to these drafting principles, the front part of prospectuses must be designed for easy reading. Text formatting and design must highlight important information for investors. Pictures, charts, graphics, and other design features may be employed for this purpose.

The plain English rules include instructions to assist in complying with the new requirements. The rules also specify the information to be provided on the front, inside, and back cover pages of prospectuses. Special requirements apply to prospectuses delivered electronically.

The staff will request that the plain English sections of prospectuses be filed in paper until the EDGAR filing system is adequately upgraded.

Requests for acceleration will not be granted unless the staff has determined that the filer has made a bona fide

About Vedder Price

Vedder, Price, Kaufman & Kammholz is a national, full-service law firm with approximately 180 attorneys in Chicago, New York City and Livingston, New Jersey.

The Corporate Securities Group

The firm's corporate finance and securities attorneys regularly represent underwriters and issuers, both foreign and domestic, in a wide variety of matters, including:

- debt and equity offerings, including initial public offerings, structured debt financings, aircraft securitizations, dual-class equity structures and sophisticated preferred stock instruments;
- capital formation, for initial capitalization, financing ongoing operations and acquisitions;
- corporate disclosure, periodic reporting, proxy solicitations, and insider trading and beneficial ownership compliance matters;
- private placement of securities including Rule 144A and Regulation S transactions;
- tender offers, mergers and acquisitions and recapitalizations and restructurings;
- international offerings of securities and compliance by foreign issuers with the U.S. securities laws; and
- litigation, administrative

effort to satisfy the plain English rules.

The staff has estimated that, in the short run, companies will experience slightly increased preparation time and added costs. Efficiencies are expected over time under the new rules.

Although suggested by commentators, no special liability safe harbors have been adopted under the plain English rules.

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STOCK OPTION REPRICINGS

The recent (and rapid) drop in stock prices has many companies considering repricing stock options granted over the last year or so.

The Financial Accounting Standards Board ("FASB") issued a preliminary interpretative opinion that repriced stock options should be accounted for under variable-plan accounting standards.

Under these standards, repriced options would be subject to mark-to-market accounting, resulting in any increase in value being booked as compensation expense. Under normal fixed-plan accounting, stock options do not result in compensation expense. Variable-plan accounting would apply to the repriced options from the date the options were modified until the date of exercise.

The FASB tentative opinion indicated that variable-plan accounting treatment would also apply if the repricing was accomplished by the cancellation of an option and the issuance of a new option grant with a lower exercise price shortly thereafter (for example, within six months) to the same individual. Similarly, variable-plan accounting would apply upon a modification of the number of shares granted under a stock option (except for adjustments caused by stock splits, stock dividends, or equity restructurings that do not increase the value of the option).

The FASB preliminary interpretation results in adverse financial accounting treatment for repriced or modified stock options. This is in addition to the detailed proxy

and arbitration proceedings involving various securities fraud claims, disclosure issues and regulatory enforcement matters.

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statement disclosure that would accompany any repricing. Companies are urged to consult with their accounting and legal advisors prior to any proposed repricings.

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