

BOWNE

DIGEST FOR CORPORATE & SECURITIES LAWYERS

ABSTRACTS OF INSIGHTFUL CURRENT ARTICLES FROM LEGAL PERIODICALS

SPINOFFS

Spin-offs, Fiduciary Duty, And The Law
By Prof. Edward Adams, University of Minnesota
Law School; and Prof. Arijit Mukherji, Carlson School
of Management, University of Minnesota
Fordham Law Review
Vol. 68, No. 1, Pgs. 15-55

Overview: *Examines the Internal Revenue Code's treatment of spinoffs. Explains its requirement for an independent business rationale to avoid taxation. Identifies non-tax deterrents to spinoffs with improper rationales, and discusses proposed Code amendments.*

Tax-free spinoffs. If a parent corporation distributes the shares of a controlled subsidiary to its stockholders as a pro-rata dividend, neither recognizes gain (or loss). IRC Section 355 makes this spinoff tax-free, provided it is not an attempt to eliminate (or reduce) taxes on extracted earnings and profits. It must have an "independent business purpose." Treasury regulations make the test a subjective one, which the spinoff fails if a practical alternative exists for achieving the avowed business purpose. Section 355(e) requires gain recognition if anyone acquires 50% or more in votes or value of the parent or sub, but not when the parent's stockholders remain the owners of over 50% in votes or value of every corporate participant in the spinoff.

Proper business rationales. Many business purposes are considered "proper" for Section 355. Stockholders can more easily monitor (and hold accountable) the management of a spinoff than that of a large public company. A spinoff of unwanted assets has been a traditional means of facilitating a merger, although Section 355(e) often makes this technique financially impracticable. Many companies raise capital by following a spinoff with an IPO. The parent might spin off a division to unlock hidden value in existing businesses and attract investors to it, particularly where that line conflicts with others or has distinct capital requirements or operating traits. A spinoff can make a company taut and focused, give feuding stockholders separate businesses to run, or let management concentrate on the core business.

Improper business rationales. To satisfy Section 355, the spinoff's rationale must be consistent with management's fiduciary duty to maximize stockholder value. Factors other than tax law may also deter a spinoff with an improper rationale. Creditors have defeated spinoffs meant to protect assets from liability under environmental statutes. A board could use a spinoff to entrench itself by making a takeover less likely. State fraudulent-conveyance laws prevent a company from intentionally hindering or defrauding creditors by spinning off one line of business with liabilities in order to protect its other lines. No tobacco holding company, for example, has dared to spin off its tobacco line in hopes of shielding its other assets.

Proposed changes. Congress erred in presuming that all spinoffs are sales; actually, few are. It could have prevented tax avoidance—without discouraging proper spinoffs—by adopting a proposal from the New York City Bar Association: tax gain only in the amount by which the spun-off entity's debt-to-equity ratio exceeds the parent's before the spinoff. Some scholars have advocated repealing Section 355(e), while the ABA has recommended amendments. For example, the definition of "plan" should include a party's intent only if that party has the authority to bring about the transaction. If the parent distributes the stock of different

IN THIS ISSUE

SPINOFFS	1
• Spin-offs, Fiduciary Duty, And The Law	
MERGERS & ACQUISITIONS	2
• Using Stock As Acquisition Consideration	
• Qualified Plan Issues Pervading 401(k) Plan Mergers	
CLOSELY HELD CORPORATIONS	3
• Slicing It Up	
SECURITIES OFFERINGS	4
• The SEC Cracks Down On Directed Share Programs	
• Public Offer Of Securities In The United Kingdom	
DUE DILIGENCE	6
• Due Diligence: The Overlooked Cornerstone	
SECURITIES LAW IN CYBERSPACE	7
• The SEC's Statutory Weaponry To Combat Net Fraud	
INDEX JULY-DECEMBER 1999	8

controlled corporations, Section 355(e) should require gain recognition only on the shares of the corporation whose ownership changes.

MERGERS & ACQUISITIONS

Using Stock As Acquisition Consideration

By Bartley Deamer

McCutchen Doyle Brown & Enersen, Palo Alto, CA

ALI-ABA Course Materials Journal

Vol. 23, No. 5, Pgs. 17-44

Overview: *Surveys the issues invoked by using stock as M&A consideration. Addresses public and private companies' concerns in deal structure and with securities law requirements.*

The risk of price changes. Merger parties using company stock as consideration must allocate the risk of stock price volatility. Targets often want the consideration measured in dollars, rather than shares. This shifts the risk of a lower stock price to the buyer. The acquiror is usually concerned about how many shares it must issue and how dilution will affect its earnings per share. It therefore prefers a fixed ratio, where it exchanges a fixed number of its shares for the target's, regardless of price. Parties can use collars to spread and limit the risk of volatility, typically one measurement (e.g., fixed value, fixed ratio) for the consideration and the other (e.g., number of shares, dollar amount) as a floor and ceiling. A more complex collar indexes stock prices to an accepted sector index (e.g., NASDAQ Computer Index) to factor out the volatility of the market itself. Often, each party can terminate the deal if the consideration goes above or below the collar amount, but the other can force the deal to proceed by limiting its consideration to the maximum or minimum collar amount.

Registration or exemption. When the acquiror issues stock to target shareholders, it must find an exemption from 1933 Act registration or avoid using unregistered securities. The parties might try an S-4 registration statement. If the deal requires corporate action by the target shareholders, the buyer must provide a written disclosure document that will act as both a prospectus under the 1933 Act and a proxy statement under the 1934 Act. Rules 134, 135, and 145(b) under the 1933 Act provide safe harbors for limited written statements before registration statement effectiveness, but target shareholders often want more.

Resales. Target shareholders must take care to avoid being classified as underwriters under Rule 145(c), because that would limit their ability to resell their shares. Often they can find an exemption under Rule 145(d), which permits resales by target affiliates so long as they comply with certain volume, manner-of-sale, and holding-period requirements. Target shareholders can resell their shares in private sales, regardless of their status under Rule 145. Some acquirors rely on the private placement exemptions, rather than registering the stock. The same principles apply to the private sale of stock in a merger as to a capital-raising sale.

Registration rights. Parties who receive unregistered stock in a merger often also get registration-on-demand rights. If the acquiror is not yet a public company, it may seek the right to delay the demand timing, so that it can control the timing of its IPO. Even if the acquiror is public, it may want the right to delay a registration-on-demand for one or two years. It might also try to limit the number of demands, for example, to one or two demands spaced a year apart. It may seek a minimum size requirement, so that the number of shares to be registered will justify its bother, expense, and exposure to liability. If the acquiror engages in more than one transaction using stock, it must coordinate between the different groups of new shareholders, controlling who has the first right to demand registration and whether other shareholder groups can piggyback on another group's demand. It must be careful to avoid a situation where the first party to demand registration has a real advantage, for this will create an artificial and premature registration demand.

Shareholder votes and agreements. Under stock exchange rules, the acquiror's shareholders must approve a merger that involves a change in control of the acquiror (e.g., by creating special voting rights in favor of target shareholders) or that increases the acquiror's stock by 20% or more. State corporate laws generally mimic these exchange rules, but with some important exceptions that could trigger shareholder voting and dissenters' rights. If the acquiror is a private company, the parties could sign a shareholder agreement addressing issues such as first-refusal rights on the sale of the company or issuance of additional stock, liquidation opportunities (such as a put upon the death of a shareholder), and board seat allocations. If the acquiror is a public company, the parties might provide for standstill rights or agree in advance how the new shareholders will vote their shares on specified issues.

Qualified Plan Issues Pervading 401(k) Plan Mergers

By Russell Gully, Thompson & Knight, Dallas, TX
Tax Management Compensation Planning Journal
Vol. 27, No. 6, Pgs. 159-167

Overview: *Highlights the common, often complex issues confronting 401(k) plan sponsors contemplating a merger of multiple plans. Discusses IRS regulations restricting or prohibiting mergers that change benefit options or vesting schedules.*

Uncharted territory. Sponsors of qualified plans must consider a number of complex issues when combining multiple 401(k) plans, without clear guidance from the IRS. Following an M&A deal, the parties often want to combine their 401(k) plans to facilitate plan administration and standardize benefits. The simple alternative would be to terminate either 401(k) and distribute its assets. Yet this may wreak havoc for the participants. IRS regulations prohibit participants in a terminated plan from participating in another defined contribution plan with the same employer for a period of 12 months following plan termination.

Preserving choices. Sponsors must first identify each plan's optional forms of benefits (e.g., lump-sum payments, installment payments, joint or survivor annuities), to ensure that plan amendments do not eliminate benefits attributable to pre-amendment service. Although the sponsors could simply allow all the participants in the merged plan to select any of the optional forms available under either prior plan, that solution may create a confusing array of benefit options. On the other hand, offering them only to participants who had it previously available would result in uneven treatment and require a number of different distribution election forms. The IRS recently acknowledged that merging qualified plans can entail greater administrative costs, because of the accumulation of various optional forms of benefits, and indicated it would propose new regulations to address this confusion.

Maintaining the status quo. 401(k) plan sponsors must also address the vesting schedules in each plan. Simply to use the most favorable vesting schedule from any prior plan may not be feasible if, for example, one of the prior plans gives full, immediate vesting. The Internal Revenue Code specifically prohibits any plan amendments that reduce the vested percentage of any employer contribution or change the vesting schedule (unless long-term participants can elect to retain the prior schedule). If an employer maintains the plan of a predecessor/employer, it must treat the participant's years of service for the predecessor as service for the surviving employer.

Avoiding discrimination. Applying the already complex discrimination testing requirements for 401(k) plans becomes even more difficult when multiple plans merge. This proves especially hard when the merger occurs in the middle of the plan year or plans with different tax years merge. Formal IRS guidance and interpretive advice regarding these requirements is paltry, and IRS representatives often encourage the use of any reasonable testing mechanism. For purposes of applying the discrimination rules, plan sponsors must determine who constitute the "highly compensated employees," not particularly difficult if the plans have common sponsorship and common plan years. With common sponsorship but different tax years, some employees may be considered highly compensated for one plan but not the other. If merged plans do not have common sponsorship, the determination of highly compensated employees should be straightforward, unless either employer made a contrary election.

Editor's Note: Another article on integrating 401(k) plans after a merger, and the complex fiduciary issues invoked, appears in "When Pensions Change Hands" by Robert Stowe England, *CFO*, August 1999, Pgs. 69-74.

CLOSELY HELD CORPORATIONS

Slicing It Up

By Fredric Tannenbaum, Gould & Ratner, Chicago, IL
Business Law Today
November/December 1999, Pgs. 52-57

Overview: *Analyzes the relationship between the majority and minority owners of a private business. Explains legal standards for minority challenges of majority actions and for majority defenses, and describes substantive areas of conflict.*

Sometimes a rocky road. The relationship between the majority and the minority owners of a private business sometimes becomes contentious. The minority might examine the majority's every action (or inaction) and, upon finding that the majority owners had favored themselves, allege a breach of fiduciary duty, bad faith, or unfair dealing. While the majority can invoke the business-judgment rule to defend their actions, they still must prove the fairness of those evidencing self-dealing or disloyalty. Even if they ultimately disprove all the allegations, they may forgo the challenged action, hoping to avoid incurring defense costs, divulging sensitive information, or being distracted again from operating the business. Minority owners might scruti-

nize the company's arrangements with other businesses that majority owners own or operate, requiring them either to refrain from dealings or prove that it is arm's-length. Similarly, the minority could challenge the compensation of key employees, especially majority owners, and make them show that their compensation is comparable to what competitors pay or what the business's other employees receive.

Areas of contention. Well-intentioned and accurate though it might be, the minority's criticism of the majority owners' business focuses (e.g., sales areas and distribution practices) can hamper operations. Inter-owner contracts seldom forbid critical input, but the majority could lessen tension and forestall litigation by giving the minority a right to approve specified key matters. Disposition of the business frequently provides a fertile ground for battle. Minority owners may allege favoritism (e.g., allocating the sale price to the majority's noncompetition or consulting agreements) or object to deal structures that—though tax-efficient—lessen cash payments. If the majority purchases the minority's interest and soon thereafter sells the business for greater value, the minority owners frequently allege fraud. One common solution is a "catch-up" clause, which increases the minority's share upon a subsequent disposition within a specified time.

Tactics to resolve deadlocks. Majority owners would like complete flexibility in using any excess cash, while the minority usually seeks payouts equal to the tax liability. A sliding scale of payouts, which increase with the business's cash flow, is often on their wish list as well. In any sale, the minority can challenge many substantive and procedural aspects but should waive any dissenters' rights they have under state law to contest the fairness of the business's sale price, which could complicate a squeeze-out merger if they own at least 10% of the company. If they hold disproportionate participation power (e.g., supermajority voting on key transactions), a deadlock could occur. Many businesses use deadlock-resolving procedures, such as dynamite rights, which permit either side to buy out the other.

Redemption and preemptive rights. When the majority owners want to form a new company without offering the minority the right to participate, the majority might have to show that the existing company could not afford to form the new one; that the new company would be dissimilar; and that the majority could properly allocate time, assets, and allegiances between the two. While the minority desires the right to dispose of its shares on terms identical with those that the majority receives, the latter should require the minority to sell on

identical terms when the buyer or the majority so directs. The minority's rights to have its interests redeemed under a preset formula might tie up cash needed elsewhere or violate lenders' covenants or state law. Minority owners might seek preemptive rights, which let them subscribe for enough additional shares to preserve their ownership percentage if the business seeks new capital, and which many states' laws do not grant.

SECURITIES OFFERINGS

The SEC Cracks Down On Directed Share Programs

By Alan Austin and Dorrian Porter, Wilson Sonsini Goodrich & Rosati, Palo Alto, CA; and Allison Bennington, BancBoston Robertson Stephens, San Francisco, CA
Insights: Corporate & Securities Law Advisor
Vol. 13, No. 9, Pgs. 2-7

Overview: Warns issuers about the securities law violations possible during an IPO if they do not carefully administer their "friends and family" program. Provides guidelines for the prudent conduct of the directed share program.

Directing the wealth. Underwriters typically allocate 5% of an IPO to a directed share program and permit issuers to identify up to 500 purchasers for the directed shares. Issuers use these "friends and family" programs to let employees and business partners join in the company's success. During the waiting period (after filing a registration statement but before it is effective), 1933 Act Section 5 forbids communicating offers to sell securities in writing, except by a prospectus meeting the requirements of Section 10(a). Rule 134(a) provides the principal exception to Section 5, allowing written communications that state only the issuer's name and a limited set of details. Issuers can use the rule to announce a directed share program, but only if a specified legend appears and a preliminary prospectus accompanies the Rule 134(a) communication.

SEC scrutiny. The Commission contends that many issuers violate Section 5 by making unlawful written communications and binding participants to a purchase before the SEC registration statement is effective. SEC examiners have begun asking issuers to describe the details of their directed share programs and provide copies of communications with participants. They are asking how participants opened then funded their purchase accounts, and how they became legally obligated to buy. If an issuer violates Section 5, the purchasers can for up to one year, rescind their transaction and

receive back their consideration paid for the stock. Some issuers have been disclosing this potential liability in their prospectus.

Practical hurdles. Some issuers and underwriters have abandoned the directed share program altogether. Issuers have trouble complying with the 1933 Act in their directed share program for several practical reasons. The interest surrounding some recent IPOs has created large programs, which are, by nature, hard to administer. Because of the expense, issuers wait until they receive at least one set of SEC comments before they print a preliminary prospectus, making the document unavailable for the early stages of the directed share program. Issuers frequently use e-mail these days to communicate with potential participants, or their websites to convey more information. These forms of electronic communications are considered “writings,” but companies seldom comply with the prospectus delivery requirements when using them. Underwriters also risk noncompliance, for example, creating contracts of purchase for directed share securities, but prior to the effective date of the prospectus. Underwriters often require purchasers to open accounts prior to the effective date, and some even require purchasers to fund the accounts before the effective date.

Guidelines. Issuers considering a directed share program should observe certain guidelines. Avoid contacting potential directed share participants in writing or by e-mail. For employees, the best approach is to hold group meetings, where an executive can explain the program. Absolutely avoid using the company website to invite participation in a directed share program. Clearly state that participants have no obligation to purchase shares until the registration statement is effective, they may not receive the number of shares they request, and they can change their minds about purchasing when the offering actually takes place. Underwriters should not implement the program until they have enough preliminary prospectuses for each potential participant. Send only the information that is necessary—the preliminary prospectus, the NASD-required questionnaire, and a brief letter explaining the

program. If the underwriter distributes the materials electronically, make certain that the participant sees the preliminary prospectus before registering interest in the program. Every communication the underwriter sends must bear the appropriate Rule 134(d) legend. Underwriters should not require participants to send funds in advance of the effective date. Finally, individuals who are subject to Section 16 short-swing trading liability must remember that they cannot flip shares until the short-swing period has expired.

The Public Offer Of Securities In The United Kingdom

By Simon Gleeson, Allen & Overy, London, England; and
Harold Bloomenthal, Holme Roberts & Owen, Denver, CO
Denver Journal of International Law & Policy
Vol. 27, No. 3, Pgs. 359-447

Overview: *Surveys the current regulatory regime for domestic and international securities offerings in the UK. Examines the impact of EU regulation and exchange listing requirements. Briefly covers antifraud liability in securities transactions.*

Multiple sources of regulation. The United Kingdom’s Financial Services Act (FSA), adopted in 1986, updated securities regulation and set separate prospectus and disclosure requirements for publicly offered securities destined for exchange listed or unlisted trading. Shortly after its enactment, however, the European Community published several directives on listing requirements (including disclosure) and public offers of unlisted securities. Adoption of the directives required modification and supplementation of the FSA structure. Consequently, three layers of regulation now exist for UK public offerings: the FSA requirements for listed securities, modified slightly in light of the EC Listing Particulars Directive; the Public Offer of Securities Regulations 1995 and the EC Prospectus Directive for unlisted securities; and an optional adaptation of the listing particulars. This last option permits later listing of securities not seeking listing when offered, whether at a later date or concurrently in another EU country.

Listing particulars. The London Stock Exchange oversees both its own and, by devolution from the

Securities Industry Board, the FSA's listing requirements. The LSE governs trading on the Exchange's principal list and on AIM (the Alternative Investment Market), a secondary facility to which the Public Offer of Securities Regulations, not the listing particulars directive, applies. British custom affects both the structure and the liabilities in an offering. Unlike in the US, underwriters do not generally purchase and resell; rather, they stand ready to purchase unsold shares at the end of the offering. For offerings to be listed requires an exchange sponsor (often the underwriter) to review the prospectus (normally identical to the listing particulars) and assure the issuer's compliance with the FSA and Exchange rules. Issuers must disclose the offering terms, business and financial condition, and the background of the issuer's directors and promoters. The financial statements may meet either UK or US GAAP or the International Accounting Standards.

Unlisted and exempt offerings. The regulations differ in several respects from the EC's prospectus directive, mostly in providing fewer or more refined exemptions from the prospectus requirement. The directive introduced an exemption for unlisted Eurosecurities offerings, chiefly Eurobond and euro equity offerings, if they are generally unadvertised. At the same time, EU member states need not give mutual recognition to an unlisted offering's prospectus, unless it conforms to the standards in the Listing Particulars Directive, so a regulations-compliant offering is valid generally only within the UK. The regulations require less disclosure detail than Yellow Book offerings and entirely exempt government securities and mutual fund interests. They exempt nonpublic offerings in the UK (without defining a public offering).

Antifraud liabilities. Under all the relevant statutory and regulatory instruments applicable in the UK, the issuer, its directors, named experts, other named responsible persons, and third-party offerors are liable for material misstatements and omissions in the prospectus or listing particulars. The laws differ subtly when describing who may sue, leading to debate over whether only someone who buys into the specific offering may sue or whether a more general fraud-on-the-market theory can prevail. The FSA provides defenses for due diligence and good-faith reliance on a named expert, and permits a claim to lapse if the plaintiff acquired the securities so long after the particulars' date that it would be unreasonable to hold the defendant to a continuing belief in their validity. The list of persons liable under the FSA excludes underwriters, but commentators

debate whether the third-party offeror language in the regulations might inadvertently include them.

Editor's Note: For more details on and developments in UK securities law, including selected portions of the FSA, regulations, LSE rules, and EU directives, see *International Securities Laws Handbook*. To order, call Bowne at 800-370-8402.

DUE DILIGENCE

Due Diligence:
The Overlooked Cornerstone
By Timothy Donovan and John Jaye
Jenner & Block, Chicago, IL
Review of Securities & Commodities Regulation
Vol. 32, No. 18, Pgs. 195-201

Overview: *Reconsiders the function of due diligence from a transactional perspective. Recommends a review and communications model that integrates business and legal issues. Furnishes a checklist of review topics and hints on how to organize information to prevent costly errors of omission.*

A holistic approach. Although due diligence in M&A practice has a bad reputation for tedium and negativity, it can, when viewed as a two-way business analysis tool, illuminate the benefits as well as the drawbacks of a transaction. Even from the seller's standpoint, this is useful, especially if the seller has to present the deal to its shareholders. The senior executives should confide their strategic objectives as early as possible to the counsel who organize and analyze data to achieve the maximum pertinent information. Even if due diligence uncovers negative information, knowledge of the strategic objectives can sometimes equip the lawyers to suggest alternative structures, which could save the deal in a different form. A large or complex transaction requires a multiparty due diligence team of outside and inside lawyers, accountants, investment bankers, management experts in operations and information technology, and legal specialists in environmental, labor, tax, and intellectual property.

Specific review areas. Although due diligence should proceed from specific knowledge of the target rather than boilerplate checklists, some areas are essential to cover in any thorough review. Among other subjects, the reviewing team should consider corporate governance and documentation; financial requirements, covenants, and accounting policies; environmental contingencies; benefit plans and other human resource issues; intellectual property and tax impacts of the trans-

action; securities, antitrust, and state antitakeover exposures; and sales, manufacturing, R&D, and information-technology practices.

Sensitive topics. The due diligence team leader should be sensitive, on the one hand, to the business objectives of the transaction and the need to communicate important issues as they arise, and on the other to the internal dynamics of the team itself. Reviewers should be alert to issues in the target's business that suggest earnings tricks, such as inventory run-ups, inter-divisional allocations and restructuring charges, as well as contingent liabilities lurking in personnel practices, tax policies, and other areas not yet the subject of reported claims. The team should also think about corporate culture and whether the merger would work between this particular buyer and seller.

Organization critical. Although data organization is important even in simple deals involving one buyer and one seller, when the transaction occurs in the setting of an auction process involving multiple interested buyers, careful organizing helps to preserve the seller's neutrality under relevant fiduciary standards. The seller should organize a data room, where potential buyers must report to request, read, and copy documents. Carefully index and segregate materials by subject matter and by sensitivity, which enables the seller to restrict certain information to only the most interested buyers. Closely monitored access—updated as necessary when delays affect the time of closing—reassures buyers, whose own fiduciary duties require that their directors have adequate information and understand the deal.

Editor's Note: This issue of the *Review of Securities & Commodities Regulation* also has an article on "Due Diligence In Asset-Backed Securities Transactions" by Andrew Katz, Pgs. 202-206. Due diligence for the acquisition of a computer company is the focus of "Web Context Ups Need For Due Diligence" by Lawrence Bell and Hilda Gilfillan, *National Law Journal*, December 20, 1999, Pgs. B6, B13-B14. For guidance on M&A due diligence, see *The Best In M&A: The Full Text Of Insightful Articles To Help You Get The Deal Done* (Second Edition). Call Bowne at 800-370-8402 to order.

SECURITIES LAW IN CYBERSPACE

The SEC's Statutory Weaponry
To Combat Internet Fraud
By Stephen Cutler and John Reed Stark
SEC, Enforcement Division
Securities Reporter
Vol. 4, No. 3, Pgs. 2-10

Overview: Describes the SEC's efforts to curb fraudulent and manipulative practices by issuers and dealers using the Internet. Notes the resurrection of dormant statutory provisions, as well as the SEC's application of standard statutory and regulatory principles to novel, Web-based marketing tactics. Highlights its proactive use of the Internet to thwart fraud.

New wine in old bottles. The SEC has not received any new statutory authority to counter fraudulent offers and sales of securities via the Internet. Instead, it has adapted its existing authority to encompass the new technologies. The chief tools at its disposal are Rule 10b-5 under the 1934 Act and Section 17(a) of the 1933 Act. Section 17(a) applies to the "offer or sale" of securities, but the SEC asserts that it can prosecute cases not involving a purchase or sale because of the "in connection with" language of 1934 Act Section 10(b) and Rule 10b-5. In *SEC v. Hoke*, which the SEC settled, the defendant abandoned his alleged scheme to spread false reports about the acquisition of PairGain, through a post on a message board linked to a website created to announce the fictitious deal, without ever having traded in the affected securities. Scalping—where parties trade a security that they themselves have recommended—is another practice seen on the Internet which, the SEC argues, falls under existing 10b-5 doctrine.

Sleeping tiger awakes. In the case of scalping and certain other Internet-facilitated touting practices, the SEC has used 1933 Act Section 17(b), a provision on which it has not often relied in recent years. Section 17(b) requires any published securities description to disclose the compensation arrangement of the person publishing the description. Despite some concern among commentators that Section 17(b) violates the First Amendment's free press and free speech clauses, the SEC has used it in situations involving Internet spamming and online message boards. In an unreported District of Columbia case, *SEC v. Huttoe* (1999), the court found that an Internet newsletter publisher had violated Section 17(b) by disclosing only that it "may" receive or trade in the recommended stocks. The court also upheld the section against constitutional challenge, noting that to require information about the publisher is not censoring the contents of the newsletter.

No such thing as a free launch. The Internet has spawned some unique forms of marketing, including tactics for selling securities. One method that raises concern is the offer of free stock in exchange for purchasing the company's products or for merely furnishing information that the offeror might later use to sell products or securities. The "offer" language of Section 5 provides the SEC an opportunity to act proactively in

securities cases before money is lost, monitoring the Internet and receiving e-mail tips from others concerning free stock and other potentially unregistered securities offerings. Under amended Rule 504 in Regulation D, no exemption exists if an issuer offers non-state-registered securities to anyone other than accredited investors, and the SEC interprets an Internet offering as being made “to the world.” The SEC has trolled the Internet for trading or sales by unregistered broker-dealers, whom it may charge with violating 1934 Act Section 15.

INDEX JULY-DECEMBER 1999

Editor’s Note: Back issues of the *Bowne Digest* are available online at www.bowne.com under the heading “Resources.”

Analyst Disclosure

Over The Wall: Handling Securities Analysts’ Conference Calls, Earnings Forecasts, And Reports Effectively, July/August, p. 2
Getting—Or Not Getting—The Word Out: Disclosure For Analysts, Investors And The Press, October, p. 1

Controlling Shareholders

Erosion Of The Law Of Controlling Shareholders, November, p. 7

Corporate Governance

From Wall Street Walk To Wall Street Talk: The Changing Face Of Corporate Governance, July/August, p. 6
The Securities And Exchange Commission And Corporate Social Transparency, July/August, p. 7
Corporate Governance Out Of Focus: The Debate Over Classified Boards, September, p. 4
Corporate Governance At The Millennium: The Decline Of The Poison Pill Antitakeover Defense, December, p. 8

D&O Duties & Liability Protection

Judicial Removal Of Directors: Denial Of Directors’ License To Steal Or Shareholders’ Freedom To Vote?, September, p. 5
Liability For Persons Signing SEC Disclosure Documents, November, p. 5
The Armor-Plated Board, November, p. 6
The Chronicling Of Corporate Minutes, Continued: A Retrospective Look At *Van Gorkom*, December, p. 7

Due Diligence

Due Diligence: Essential Tips For Acquirers Of Technology Assets, November, p. 3
Author Update On IP Due Diligence, November, p. 8

Executive & Stock Compensation

Executive Compensation And Employee Benefits In Mergers And Acquisitions: Trends And Developments, October, p. 4
No Fool For A Client: The Finance And Incentives Behind Stock-Based Compensation For Corporate Attorneys, October, p. 5
Executive Compensation And The Misplaced Emphasis On Increasing Shareholder Access To The Proxy, November, p. 4

Fiduciary Duties

The Trusts And Estates Lawyer, The Investment Process, And Selected Securities Law Issues, September, p. 8

Global Securities Regulation

Securities Markets And Securities Regulation In China, October, p. 7
Euro And Company Law, October, p. 8
Disclosure In Global Securities Offerings: Analysis Of Jurisdictional Approaches, Commonality And Reciprocity, December, p. 5

Insider Trading & SEC Investigations

Avoiding Insider Trading Liability When Selling Company Stock, July/August, p. 3
Lying To The SEC: The Basics Of The False Statements Statute, July/August, p. 4

Investment Bankers

Liability Of Investment Banks For Providing Financial Advice, December, p. 3

Mergers & Acquisitions

Employment Law Issues In Mergers And Acquisitions, September, p. 3
Hot Topics In Antitrust Review Of Transactions, September, p. 3
Negotiating Acquisition Agreements, November, p. 3
The Immigration Consequences Of Mergers, Acquisitions, And Other Corporate Restructuring: A Practitioner’s Guide, December, p. 1
Information Sharing In The Pre-Merger Context: How To Avoid Antitrust Liability, December, p. 2

Securities Disclosure

When Corporate Managers Fear A Good Thing Is Coming To An End: The Case Of Interim Nondisclosure, July/August, p. 1
Plain English Comes To M&A Disclosure, July/August, p. 2
To Tell Or Not To Tell: Reassessing Disclosure Of Uncharged Misconduct, September, p. 1
Update On Forward-Looking Statements And The Reform Act Safe Harbor, October, p. 2
Disclosure, Intellectual Capital And Value In The Internet Age, October, p. 3
Company Disclosure Of Earnings Projections: Should Individual Investors Be Allowed Into The “Ball Park”?, October, p. 3

Securities Fraud

The Resurrection Of The Dodo: The Unfortunate Re-emergence Of The Puffery Defense In Private Securities Fraud Actions, September, p. 2
Defining The Duty: Attorneys’ Obligations Under Rule 10b-5, December, p. 4
Disgorgement: A Primer, December, p. 6

Securities Law In Cyberspace

Avoiding Securities Law Liability For A Company’s Web Site, July/August, p. 5
Corporate Web Disclaimers: To Disclaim Or Not To Disclaim, It Should Not Be A Question, November, p. 1
Observations On Corporate Websites And The Federal Securities Laws, November, p. 2

Securities Offerings & Distributions

Small Issue Public Offerings Conducted Over The Internet: Are They “Suitable” For The Retail Investor?, September, p. 6
Distributions Of Thinly Traded Stocks: The Legal Perspective, September, p. 7
Playing The Stock Market: “Going Public” And Professional Team Sports, October, p. 6

Editor’s Note: *The October, November, and December 1999 issues were misnumbered as Volume 14. The correct volume number is 13. We apologize for any confusion this may have caused.*