

SCHNEIDER WEINBERGER LLP

MEMORANDUM

To: CLIENTS

FROM: SCHNEIDER WEINBERGER

DATE: JUNE 24, 2004

RE: SEC'S PROPOSED RULES APPLICABLE TO SHELL COMPANIES

The SEC has proposed new rules that would change existing Form 8-K filing requirements, and restrict the use of Form S-8 registration statements, for companies deemed by the SEC to be "shell companies." These rules have particular application to operating companies effecting business combinations with public shell companies.

Definition of Shell Company

Under the proposed rules, a "shell company" would be defined as a company "with no or nominal operations, and with no or nominal assets consisting solely of cash and cash equivalents".

Types of Transactions Covered

The proposed rule covers transactions between a shell company and an operating business (a "Covered Transaction") in which:

- The shell company acquires the operating business (known as a "reverse merger or acquisition"); and
- The operating business acquires the shell company and succeeds to the public company status of the shell company (known as a "back-door merger").

Form 8-K

Under the proposed rules, a shell company must provide certain information under a Current Report on Form 8-K within as few as four business days following consummation of a Covered Transaction (once the new rules concerning Form 8-K become effective in August 2004).

The information that must be provided includes information about the operating company equivalent to the information that would be required to be filed under an Exchange Act registration statement. This information would include information about the operating

company's business, management, principal shareholders and financial condition (including the audited financial statements of the operating company) sufficient to enable investors to make an informed decision whether to buy or sell the former shell company's securities ("Required Disclosure").

Previously, the required financial statements (and pro-forma financial information) could be provided up to 75 days from the closing date of the Covered Transaction (or 60 days following the filing of Form 8-K reporting closing of the Covered Transaction). If this provision is adopted as proposed, completion of Covered Transactions mergers involving shell companies will have to be delayed until the Required Disclosure becomes available.

Form S-8

Under the proposed rules, a shell company may not use Form S-8 to register its shares issuable under company-wide or individual equity compensation plans, including upon exercise of options, until (a) 60 days after the shell company ceases to be a shell company in a Covered Transaction, and (b) the former shell company has filed Required Disclosure. The Required Disclosure would be filed under a Form 8-K or in registration statement filed on Form 10(SB).

Conclusion

The purpose of the proposed rules is to require reporting shell companies that acquire (or are acquired by) an operating business to provide adequate financial and other information to the investment community so that they are able to evaluate whether to purchase or sell the shell company's securities. Under existing rules, a reporting shell company can defer for up to 75 days, the filing of financial information about the newly acquired operating company. And, it may defer until its next annual report on Form 10-K(SB), the disclosure of other material information about the business, management and shareholders of the operating company.

While the benefits of the current rules are enjoyed by many of our clients, it was just a matter of time before the SEC closed the "loophole."

As is the case with most new SEC proposals, they have been published and comments have been requested. For your information, we have submitted a comment on the proposed rules. If the proposed rules are adopted, they may not be adopted in the form that they have been proposed.

We will keep you apprised of the status of these proposed SEC rules, but, in the interim, please contact us with any questions or comments.

SIW:sjm