Nasdaq Delisting: Process, Implications and Strategies September 28, 2001

Recent market declines have caused the common stock of many companies to face delisting from the Nasdaq National Market (the "NNM").

In addition to the NNM, Nasdaq operates the Nasdaq SmallCap Market ("SmallCap"), and the National Association of Securities Dealers, Inc. ("NASD") operates the over-the-counter electronic bulletin board ("OTCBB"). In order for the stock of a company to be traded on the SmallCap, the issuer must meet minimum listing criteria that are less demanding than the corresponding NNM criteria. The stock of any company in compliance with its SEC reporting obligations can be traded on the OTCBB, but only market makers (and not issuers) can apply to quote securities on the OTCBB. As of June 30, 2001, there were 3,570 stocks traded on the NNM, 803 stocks traded on the SmallCap and 3,451 stocks traded on the OTCBB. Approximately 6,000 stocks also trade on the Pink Sheets, a largely unregulated electronic market that is not operated by Nasdaq or the NASD.

Listing Standards

Nasdaq's new and former minimum standards for continued listing on the NNM and the SmallCap are attached to this memorandum. Nasdaq's new maintenance standards, which became effective on June 29, 2001, changed the net tangible assets standard into a shareholders' equity standard for both the NNM and the SmallCap and lowered the minimum bid price under maintenance standard 2 for the NNM from $5.00 to $3.00 per share. Until November 1, 2002, companies may qualify for continued listing under either the new or former maintenance standards. Beginning November 1, 2002, companies must comply with the new maintenance standards.

Delisting Process

The Nasdaq delisting process generally proceeds as follows:

Deficiency Notice. If a company does not meet the minimum bid price or market value of public float requirements for 30 consecutive trading days, Nasdaq sends a "deficiency notice" identifying the listing deficiency and informing the company that it will be delisted after 90 calendar days unless it meets the required minimum bid price or market value of public float for at least 10 consecutive trading days during the 90-day cure period. If the deficiency is based on insufficient market capitalization, the company is notified after 10 consecutive trading days of non-compliance and must achieve compliance for 10 consecutive trading days within 30 calendar days. Nasdaq employs an automated computer system to track compliance by each listed company with these requirements. If the deficiency is based on insufficient net tangible assets (former maintenance standards), shareholders' equity (new maintenance standards), total assets, total revenue or pretax income, the notice is usually triggered by public filing of an SEC report (typically a Form 10-K or 10-Q) disclosing the deficiency.

Determination Letter. If the company is not in compliance within the time period prescribed in the deficiency notice, Nasdaq sends a "determination letter" informing the company that Nasdaq

has determined that the company does not meet the standards for continued listing. The company then has seven calendar days to appeal the determination. Under Nasdaq rules, the company must publicly announce within seven calendar days that it has received a determination letter and the basis for the delisting.

Appeal to Nasdaq Panel. The company's appeal may be made through a written submission to, or at an oral hearing before, a Nasdaq listing qualifications panel of two or three persons selected by Nasdaq. The panelists are independent representatives of the business community and cannot be employees of the NASD or any of its subsidiaries. If an oral hearing is requested, it is generally held within 45 calendar days. The company must pay a fee of $5,000 for an oral hearing and $4,000 for a written appeal.

Plan of Compliance. In the appeal, company representatives present a "plan of compliance" — the company's plan to achieve and sustain compliance with the Nasdaq maintenance standards. Without a credible plan, delisting is usually swift and certain. The mere assertion that the company believes its stock will trade above the minimum price is insufficient.

Decision. The Nasdaq panel renders its decision, typically within two to four weeks after the written submission or hearing. If the decision is to delist, the delisting becomes effective at the close of trading on the day the company is informed of the decision.

Further Appeals. The company may appeal the Nasdaq panel's delisting decision to the Nasdaq Listing and Hearing Review Council within 15 calendar days, and the Review Council may on its own motion elect to review any decision within 45 calendar days. The NASD Board of Governors may, in its discretion, review any decision by the Review Council. Aggrieved issuers may also appeal any Nasdaq decision to the SEC or federal court. Appeals beyond the Nasdaq panel do not stay delisting and are rarely pursued.

Delisting Moratorium

On September 27, 2001, Nasdaq suspended its minimum bid and market value of public float requirements for continued listing until January 2, 2002. During this moratorium, Nasdaq will not delist any company for failure to meet these requirements.

Delisting Implications

Delisting has a number of negative implications, depending on whether the company is delisted to the SmallCap or OTCBB as well as company-specific factors:

Covenants. Delisting may violate covenants contained in the company's equity or debt agreements, such as registration rights agreements, stock purchase agreements, preferred stock terms, warrant agreements, indentures or bank credit agreements.

Blue Sky Laws. A company trading on the SmallCap or OTCBB cannot avail itself of federal preemption of state securities laws, also called "blue sky" laws, for issuer transactions. As a result, the company's securities must either be registered or exempt in each applicable state.

Although there are a number of available exemptions, they vary from state to state. As a result, the blue sky laws of each state need to be examined with respect to continued trading in the delisted company's outstanding securities and for each proposed issuance of securities, including pursuant to employee option plans, stock purchase plans and private or public offerings of securities.

Form S-3 Eligibility. There is no impact on a company's eligibility to use Form S-3 if it is delisted to the SmallCap so long as it continues to meet the Form S-3 eligibility rules for the particular type of transaction proposed. For example, one requirement for primary offerings (but not secondary offerings on behalf of selling stockholders) on Form S-3 is that the issuer's public float must exceed $75 million. On the other hand, a company transferred to the OTCBB loses S-3 eligibility for all purposes if its public float does not exceed $75 million. Loss of S-3 eligibility is significant because it results in the inability to automatically incorporate information contained in subsequent SEC filings into most registration statements, thereby increasing the burden of keeping registration statements current. Subsequent SEC filings will, however, continue to be automatically incorporated into Form S-8 registration statements covering employee benefit plans.

Rule 144 Sales. A listing transfer to the SmallCap does not affect the operation of Rule 144. However, the market-based volume limitation set forth in Rule 144(e) is not available for securities quoted only on the OTCBB. Delisting to either the SmallCap or OTCBB does not affect the availability of Rule 144(k), which greatly facilitates the ability of non-affiliates of a company to publicly resell stock that they acquired in a private placement and have held for at least two years.

Margin Loans. If a company is delisted to either the SmallCap or OTCBB, its common stock is no longer eligible for margin loans.

Penny Stock Rules. A company trading on the SmallCap is not subject to the SEC's penny stock rules. However, if listing is transferred to the OTCBB the company becomes subject to the penny stock rules unless its average annual revenue in the preceding three years exceeds $6 million. If applicable, the penny stock rules impose additional disclosure and sales practice requirements on broker-dealers who sell such securities to persons other than established customers and "accredited investors".

Liquidity. As a result of the loss of market efficiencies associated with the NNM and the loss of federal preemption of state securities laws, delisting from the NNM to the SmallCap generally reduces liquidity in the stock. The market liquidity is further reduced if the stock is transferred to the OTCBB.

Nasdaq Corporate Governance Requirements. A company delisted to the SmallCap must still comply with Nasdaq's corporate governance requirements, including Nasdaq's stockholder approval and audit committee requirements. A company transferred to the OTCBB need no longer comply with Nasdaq's corporate governance requirements.

California Corporate Law Considerations. If a company is incorporated in California or is based in California (regardless of where it is incorporated) or meets the other jurisdictional tests which make it a "deemed California corporation", then there are significant corporate law implications that could necessitate changes to the company's charter, bylaws, proxy materials and stockholder voting procedures if the company is delisted from the NNM. These include, among other things, requirements for the annual election of directors and annual stockholder meetings, limitations on corporate distributions, cumulative voting rights for stockholders, dissenters' rights and limitations on supermajority voting provisions.

Other Factors. Delisting from the NNM — especially to the OTCBB — can result in a loss of confidence by suppliers, customers and employees, the loss of analyst coverage and institutional investor interest, fewer business development opportunities and greater difficulty in obtaining financing.

Strategies to Avoid Delisting

Many companies accept delisting, especially if there is fundamentally nothing the company can do to prevent it. Others choose to fight delisting, employing different strategies depending on the nature of the non-compliance.

If delisting is initiated because of a low stock price, a reverse stock split or stock repurchase program can increase the stock price. A stock repurchase can usually be implemented more quickly because it does not require stockholder approval, but it consumes cash. Neither technique is certain to provide a long-term fix, since stock prices often drift back downward after a reverse split or buyback.

If delisting is predicated on an inadequate market cap or public float, a reverse stock split or stock repurchase will not help, and can even hurt if it reduces the number of shares held by non-affiliates below the required minimum.

Another possible response to a low stock price is to cut expenses, pursue new strategic relationships or major contracts or otherwise improve the business, hoping that improved profitability will increase the market price. In reality, this is easier said than done and usually cannot be accomplished in time to stave off delisting.

Finally, Nasdaq companies trading above $2.00 per share may wish to consider a dual listing on the Boston Stock Exchange ("BSE"). A company listed on the BSE retains its Form S-3 eligibility and gains some additional "blue sky" exemptions. In addition, unlike Nasdaq, the BSE does not have any continued listing standards and will not delist a company's stock based on its trading price, market capitalization, public float or other trading parameters. The BSE's current initial listing fee is $7,500 with an annual fee of $1,000.

David A. Westenberg
Patricia A. Whalen

FORMER NASDAQ MAINTENANCE STANDARDS[1]

Nasdaq National Market

Standards	Maintenance Standard 1	Maintenance Standard 2
Net Tangible Assets[2]	$4 million	N/A
Market Capitalization Total Assets Total Revenue	N/A	$50 million OR ($50 million AND $50 million)
Public Float (shares)[3]	750,000	1.1 million
Market Value of Public Float	$5 million	$15 million
Minimum Bid Price	$1.00	$5.00
Round Lot Shareholders[4]	400	400
Market Makers	2	4
Corporate Governance	Yes	Yes

Nasdaq SmallCap Market

Net Tangible Assets Market Capitalization Net Income (most recently completed fiscal year or 2 of the last 3 years)	$2 million OR $35 million OR $500,000
Public Float (shares)	500,000
Market Value of Public Float	$1 million
Minimum Bid Price	$1.00
Market Makers	2
Round Lot Shareholders	300
Corporate Governance	Yes

[1] Until November 1, 2002, companies may qualify for continued listing under either the new or former standards.
[2] Net Tangible Assets equals Total Assets minus Total Liabilities minus Goodwill minus Redeemable Securities.
[3] Public Float is defined as total shares outstanding less any shares held by officers, directors or beneficial owners of 10% or more.
[4] Round lot shareholders are holders of 100 shares or more.

NEW NASDAQ MAINTENANCE STANDARDS[1]

(Changes are highlighted in **bold**)

Nasdaq National Market

Standards	Maintenance Standard 1	Maintenance Standard 2
Shareholders' Equity	**$10 million**	N/A
Market Capitalization Total Assets Total Revenue	N/A	$50 million OR ($50 million AND $50 million)
Public Float (shares)[2]	750,000	1.1 million
Market Value of Public Float	$5 million	$15 million
Minimum Bid Price	$1.00	**$3.00**
Round Lot Shareholders[3]	400	400
Market Makers	2	4
Corporate Governance	Yes	Yes

Nasdaq SmallCap Market

Shareholders' Equity Market Capitalization **Net Income**[4] (most recently completed fiscal year or 2 of the last 3 years)	**$2.5 million** OR $35 million OR $500,000
Public Float (shares)	500,000
Market Value of Public Float	$1 million
Minimum Bid Price	$1.00
Market Makers	2
Round Lot Shareholders	300
Corporate Governance	Yes

[1] Until November 1, 2002, companies may qualify for continued listing under either the new or former standards.
[2] Public Float is defined as total shares outstanding less any shares held by officers, directors or beneficial owners of 10% or more.
[3] Round lot holders are holders of 100 shares or more.
[4] **Excluding extraordinary or non-recurring items.**