STATE OF NEW YORK DEPARTMENT OF LAW — OFFICE OF ATTORNEY GENERAL ROBERT ABRAMS

MEMORANDUM

TO: REF Attorneys and Paralegals DATE: 2/6/90

FROM: Mary Sabatini DiStephan

RE: Change in Sponsors' Financial Condition

Many attorneys and paralegals have been asked by sponsors and their attorneys when they must amend a plan in order to disclose a change in financial position of a sponsor or holder of unsold shares. This is a matter of great concern to sponsors in this soft real estate market.

I am writing this memo to reiterate the requirements of the Martin Act, our regulations and case law about when a plan must be amended.

All material facts must be disclosed in the offering plan. General Business Law § 352-e(1)(b), 13 NYCRR 18.1(b), 23.1(b). In State of New York v. Rachmani Corp., 71 NY2d 718 (1988), the Court of Appeals adopted the TSC Industries v. Northway (426 US 428) standard for what constitutes a material fact of an offering - a showing of a substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder. Thus, the court analyzed there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the "total mix" of information made available.

Any adverse change in the sponsor's net worth which made its original affidavit, submitted pursuant to 13 NYCRR 18.2(c)(d)(D-4) and 13 NYCRR 23.2(c)(d)(D-4), no longer accurate, would require an immediate amendment. The affidavit requires the sponsor to represent that its net worth is or will be sufficient to meet the requirements of GBL Section 352-k and to cover all the unsecured obligations sponsor assumes in the offering plan, including sponsor's obligation for unsold shares or units.

Likewise, any circumstance which would jeopardize the ability of the sponsor to perform its obligations under the offering plan -- to pay maintenance; to make payments on underlying mortgages; to fund a reserve fund; to make repairs or capital improvements to the building; or any other promise -- would require immediate amendment. This amendment should be filed as soon as a sponsor becomes or should be aware of the problem. Clearly a default on a mortgage or taxes, a sponsor's failure to pay maintenance, or the initiation of a foreclosure or bankruptcy action would trigger an amendment. But, before any such drastic event occurred, a sponsor must or should have been aware of a problem, and it is at that earlier time that an amendment is required.

Any lien or lis pendens or any litigation pending against the building is also a material fact which must be disclosed in an immediate amendment.

Sponsors and their attorneys should be cautioned to err in favor of disclosure at the earliest possible time in order not to be liable for failure to make adequate and timely disclosure of material facts.

We are currently studying other disclosures which may be appropriate.

Please see me if there is any question or problem.

MSD:kd