Going with the cash flow

Get to know this crucial factor in communications deals

By FREDRIC D. TANNENBAUM

Operating cash flows and the broadcast and telecommunications industries: Are you ready to deal?

A confluence of factors, in near perfect alignment, has dramatically accelerated the trends toward consolidation in the broadcasting and telecommunications industries. Structural changes legislated by the Telecommunications Reform Act of 1996, an economy enjoying seven years of uninterrupted growth (until the recent downturn caused by the Asian depression), access to capital by virtue of very strong debt and equity markets, and managements' real or perceived desire for economies of scale and scope have all contributed to the extraordinary wave of mergers and acquisitions.

The size and number of these transactions is unprecedented. In the radio industry alone, according to government statistics, 4,000 of the 11,000 stations in the United States have changed ownership in the less than two years since the passage of the reform act, including more than 1,000 mergers, and more than 140 transactions requiring a Hart-Scott-Rodino filing. Three of the five largest mergers in corporate history have occurred in the telecommunications industry, including the recently completed $37 billion WorldCom-MCI combination, the pending $62 billion SBC-Ameritech merger and the $63 billion Bell Atlantic-GTE pending transaction.

Consolidation in the communications industry introduces a lawyer to unique jargon. Shorthand like POPs, MTAs, BTAs, MHz, OCF, EBITDA, PCS, SMR, Dbu, UHF, VHF, AM, FM, FCC, RBOCs, CLECs, LECs, LMA and CPM conjure up an alphabet soup of terms that causes even the most attentive eyes to glaze over. Transactions in this industry also sensitize a lawyer to a distinctive amalgam of legal and business issues.

One fundamental business concept is central to every communications acquisi-

Tannenbaum is a partner with Gould & Ratner in Chicago.

Tim Lee

Slicing it up

Should a majority owner sell a piece of the pie?

By FREDRIC D. TANNENBAUM

Ma & Pa Inc. is looking for some partners — but the owners still want to be in charge.

After all, many private business owners sell (or grant options to sell) minority ownership interests in their business to employees, investors, family members, friends and others. The majority owner selling these minority interests may be motivated by many reasons, such as: the desire to obtain new capital, incentivize, reward or put "golden handcuffs" on employees, strive for family harmony, obtain estate planning goals and reap the emotional feeling of power or largesse.

The majority owner's goals, while certainly well intended and understandable, often focus only on these positive aspects, but seldom factor in the countervailing concerns that will be addressed in this article. This article in no way attempts to dissuade business owners from inviting minority partners or minority owners eagerly accepting ownership.

Rather, the purpose here is to assist the majority owner in carefully weighing the risks inherent in sharing the business' profits and losses, financial and other confidential information and opinions regarding the future direction of the business with minority owners. At the same time, it attempts to outline certain inherent risks faced by minority owners whose fortunes may be subject to the caprice and creativity of the majority.

While many, if not most, majority and minority owners co-exist amicably, the cases of unhappy relationships and their ultimate unwinding sometimes overshadow, and certainly receive more notoriety, than the positive examples.

This article points out various factors that majority owners should consider before granting stock options or selling stock in their businesses to minority owners. It also serves to heighten minority owners' awareness of some of the risks inherent in minority ownership that will become apparent once the bloom is off the rose. The principles set forth apply to every form of business enterprise, whether a corporation, partnership or limited liability entity, even though some principles will be more salient in certain forms.

Overall fundamental fairness/exercise of fiduciary duty. A vigilant or persistent minority owner will be entitled to scrutinize carefully every action or inaction by the majority owners. These rights exist, within reasonable limits, whether the minority owner sincerely questions the majority's conduct or is trying to use its position to frustrate or hinder the majority.

In general, minority owners may assert that the majority breached its fiduciary duty or engaged in bad faith and unfair dealing and other contractual breaches based on various fact patterns. To support those legal conclusions, minority owners will seek to weave a tapestry of facts showing that the majority regularly or systematically, or at least occasionally, favored itself over the best interests of the business or the minority.

The business-judgment rule will often sanitize many of the majority's actions. The rule generally states that the majority's good-faith decisions regarding management issues or the overall stewardship of the entity are presumed to be valid and not actionable.

However, acts of self-dealing, disloyalty or self-preference shift the burden back to the majority to prove its "fairness." While the majority may ultimately prevail on all charges, the

Tannenbaum is a partner at Gould & Ratner in Chicago and is chairman of LawExchange International.

Amy Young