LB-40

CONFIDENTIAL DRAFT

Memorandum to Mr. Forrest Shumway

Considerations Relating To The

Signal Companies Investment In UOP

LEHMAN BROTHERS
INCORPORATED

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EXHIBIT "C"

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PHILIP D. ROSS, N. P.
(Shumway Depo.)

I. Introduction and Conclusion

This memorandum discusses the advantages and disadvantages of Signal's acquiring the remaining 49.5% public minority interest in UOP during the remainder of 1976. There are complicated legal, business and financial considerations involved, but it is timely to consider them now and, hopefully, this related analysis will be helpful to Signal.

Our recommendation is that Signal seriously consider acquiring 100% ownership in UOP over the medium term future. The following discussion provides both our reasons for this judgement and an analysis relating to the appropriate purchase price and currency.

It is Lehman Brothers' understanding that Signal, after having purchased 50.5% of UOP in April 1975, had no specific plan to acquire the remaining 49.5% interest at the soonest practicable date. In our judgement, though, certain developments have occurred since last April which make it timely for Signal management to consider this acquisition now.

Based on our analysis of other multiple-phase acquisitions, and factors relating specifically to Signal and UOP, it is Lehman Brothers' judgement that Signal should be prepared to pay between $17 and $21 per remaining UOP share to acquire 100%

control. Within this price range, Signal should be able to structure this acquisition so as to positively effect its earnings per share.

II. The Benefits of Signal Owning 100% of UOP

We think, in general, that 100% ownership of an attractive business is preferable, from the owner's standpoint, to a lesser equity position. The traditional cash flow, disclosure, management control and other reasons for this viewpoint seem applicable in this instance. The following section outlines these major reasons as they apply to Signal and UOP.

1. It appears to us that UOP's basic businesses, i.e., Process and the Manufacturing Groups, are sound and have long term earnings growth potential. Moreover, over the near term, these businesses clearly are improving. Accordingly, despite UOP's 1975 losses, we think that Signal's earnings per share trend would benefit from 100% ownership of UOP. Furthermore, Signal's estimated 1976 earnings per share should increase if a non-dilutive form of acquisition is structured. Section III-B on page analyzes alternative forms of structuring and financing the purchase of UOP shares.

2. UOP's current stock price is undoubtedly effected by investor concern with UOP's 1975 deficit and therefore may be undervalued in relationship to these future earnings prospects. While it is difficult to predict stock price movements, if the current market upswing continues, it is likely that investors will begin to ascribe higher market values to UOP.

3. Furthermore, 100% ownership of UOP may enable Signal to manage UOP more effectively, as a result of eliminating the public minority interest. As management knows, the parent of a subsidiary with substantial public ownership may not be able to fully consolidate the two companies' business strengths (e.g., intercompany licensing and marketing arrangements) because of the necessity of maintaining arms length relationships. Given the overlap in certain UOP and Signal businesses, particularly between Garrett, Procon and Process, the ability to maximize such relationships may be important to Signal. In addition, Signal management will no longer have to be concerned with separate disclosure requirements for UOP.

4. From a tax standpoint, UOP has approximately $20.4 million of loss carryforwards as a result of its 1975 losses. As the management of Signal well understands,

such carryforwards may not be utilized by Signal unless it owns at least 80% of the common stock of UOP and files a consolidated tax return. In addition, it is likely that Signal will be able to flow the related tax benefit through its income statement by reducing the goodwill created by the UOP acquisitions. This could result in approximately a $.03 annual boost in Signal's earnings per share over the next 40 years. Additionally, pro forma for 100% ownership, Signal will not have to pay any taxes on the dividends it receives from UOP. Currently, it must pay taxes at the 7.2% rate.

5. Signal also might benefit from the increase in its common stock "float" which would result from exchanging new shares for the balance of UOP. We realize that Signal and Gulf & Western recently completed a joint tender offer whose objective was exactly the opposite - namely to reduce Signal's equity capitalization. Nevertheless, it may serve Signal, from a defensive standpoint, to re-issue some of this equity today.

The major possible negative for Signal would be an unfavorable reaction in the investment community to any further investment in UOP. As management well knows, UOP's disappointing 1975 results have led certain analysts to question Signal's original investment. In our opinion, however, the turnaround in UOP's business and the related tightening of Signal's control will ultimately change investor perception of UOP and the wisdom of Signal's having acquired it. On balance, we think that the financial and qualitative considerations discussed above outweigh this negative.

III. Analysis of the Costs and Method of Obtaining 100% Ownership In UOP

Assuming that Signal management believes that 100% ownership of UOP is attractive, it then makes sense to analyze the price and terms under which the remaining 49.5% public interest might be acquired. The following sections discuss these considerations and, specifically, the effects of alternative combinations of cash, stock, and debt on Signal's financial statements.

A. Considerations Relating To The Price Which Signal Should Offer UOP Shareholders

Introduction

The obvious starting point for any company considering the second phase of a two-step acquisition is the price paid to acquire its initial interest. While financial and market conditions may dictate otherwise, there is a strong body of legal advice which suggests that any second phase offer below the price offered in the initial phase will create the risk of material litigation. While Lehman Brothers clearly cannot advise Signal on these litigation risks, they must be studied carefully.

This section, however, will set forth the considerations which, from a business and financial viewpoint, might support an offer to UOP shareholders within the $17 - $21 range. We have not attempted to select a particular price which we think would be fair to the UOP shareholders. We have, instead, focused on this range within which a transaction might successfully be negotiated.

Table I on page 7 sets forth current market data for Signal and UOP as well as a summary of the 1975 tender offer.

Table I

Summary Fact Sheet for The Signal Companies, Inc. and UOP Inc.

	The Signal Companies, Inc.	UOP Inc.
I. Summary Market Data		
Current Price (6/21/76)	$ 21 1/4	$ 12 1/4
1976 Range	$22 3/8-15 3/8	$13 5/8-10
1975 Range	18 3/4-13 7/8	18 - 9 1/2
1970-1974 Range	27 1/8-12 3/4	36 3/4-9 3/4
Dow Jones Industrial Average (6/21/76)	1002	
1976 Est. E.P.S.	$2.90	$1.30
Latest 12 Months E.P.S.	1.96	(3.36)
1975 E.P.S.	1.82	(3.19)
1975 Book Value per Share	40.82	15.70
Price to:		
1976 Est. E.P.S.	7.3x	9.4x
Latest 12 Months E.P.S.	10.8x	(-)
1975 E.P.S.	11.7x	(-)
1975 Book Value	.53x	.78x
Indicated Dividend	$.90	-
Indicated Yield	4.3%	-
Shares Outstanding (000)	19,749	5,725(a)
Market Value ($MM)	$419.7	$69.0
II. Prior Signal Offer For UOP Inc.		
Date		4/21/75
Dow Jones Industrial Average		808
Shares Sought		4,300,000
Tender Price		$21
UOP Price Prior to Offer		$13 7/8
UOP 1975 Price Range Prior to Offer		$14 1/8-10 1/8
UOP Price Prior to Offer to:		
1975 Est. E.P.S.		5.7x
Latest 12 Months E.P.S.		5.3x
1974 E.P.S.		4.7x
1974 Book Value		.69x
Premium of Signal Offer over UOP Price		63%
Shares Tendered		7,800,000
Shares Accepted		4,300,000

a) Shares not owned by Signal.

Offers Made in Other Multiple Stage Acquisitions

Table II on page 9 presents data relating to recent multiple stage acquisitions. Included are a significant number of acquisitions in which the second offer was lower than the initial offer. While none of the situations are precisely analogous to Signal/UOP, (e. g., none of the companies underwent an earnings decline of UOP's magnitude) the table does indicate that successful multiple phase acquisitions have occurred with lower second-phase offering prices. It seems to us, therefore, from an investment banking standpoint, that Signal can consider prices below its 1975 tender offer price.

Table II

Selected Tender and Exchange Offers Related to Multiple-Stage Acquisitions

		Ownership			Market Data									
:ompany/ l Company	Date	% Owned Prior to Offer	% of Shares Offered for	Market Value of Offer ($ mil.)	Market Price Per Share Before Tender	Tender Price	Market Premium	Ratio of Second Price to First Price	S & P 425 Index	Latest 12 Months' EPS	Tender Price to Latest 12 Months' EPS	Number of Shares Offered for (000)	Number of Shares Tendered (000)	Remarks:
:td. /	11/15/73	--	51.0%	$ 60.8	$11 5/8	$19.00	63.4%	--	115.13	$ 1.28	14.8x	3,200	5,210	* Market value of $18 pri
alon Co.	11/14/75	51.0%	30.6	29.1	11 5/8	15.30*	31.6	0.80x	101.88	deficit (a)	deficit (a)	1,900	1,873	Debentures of 2000.
;ar Co. Inc. /	6/23/75	--	100.0	25.2	10	13.25	32.5	--	104.88	deficit	deficit	1,900	1,629	* Market value of $15 pri
roducts	8/27/75	86.0	14.0	3.6	9 1/8	13.25*	45.2	1.00x	94.76	deficit	deficit	272		Debentures.
:p. /	7/10/74	--	30.0	31.0*	18 1/2	25.00	35.1	--	90.34	4.31	5.8x	1,241	1,241	The initial purchase was n
:p.	9/ 8/75	30.0	24.0	23.0	18 1/8	23.00	26.9	0.92x	96.36	4.42	5.2x	1,000	1,242	* The market value of cash
;ine Kuhlmann Corp. /	10/24/73	55.0	9.3	21.5	16 3/4	21.50	28.4	--	124.06	1.39	15.5x	1,000	2,720	
Corp.	7/10/75	70.0	30.0	61.3	15 3/8	19.00	23.6	0.88x	106.30	2.14	8.9x	3,228	2,475	
ood Specialties, Inc. of Nestle Alimentana)/ McNeill & Libby	5/30/75	61.0	39.0	30.5	4 7/8	8.125	66.7	N/A	102.65	1.05	7.7x	3,768	2,910	
ergy Corp. /	4/30/70	--	51.0	83.2	N/A	12.81	N/A	--	82.57(b)	N/A	N/A	6,500	6,500	Initially purchased newly i
ean Oil, Inc.	9/30/74	53.5	46.5	70.7	9 5/8	12.00	24.8	0.94x	63.54(b)	0.49	24.5x	5,889	4,215	ocean in connection with a
:ls & Chemicals/	3/11/74	--	23.0	21.0	23 7/8	30.00	25.7	--	110.62	2.60	11.5x	700	1,150	
:cial Solvents	6/28/74	37.3	9.8	9.0	24 7/8	30.00	20.6	1.00x	97.39	3.45	8.7x	300	283	
)rnemisza/	9/27/73	--	20.6	29.7	19 3/4	27.00	36.7	--	109.08(b)	3.47	5.7x	1,100	1,213	
ead	7/15/74	34.0	66.0	156.4	21 3/4	27.00	24.1	1.00x	83.78(b)	3.61	6.0x	3,830	3,310	
	2/11/76	90.6	9.4	17.6	.23	30.00	30.4	1.11x	100.77(b)	3.12(c)	9.6x(c)	586		
ıds/	5/22/73	39.8	14.4	7.8	15 1/2	25.00	61.3	--	114.77	2.88	8.7x	--	312	34.6% of shares previousl
;rant	4/12/74	54.2	20.0	6.8	27 3/4	34.00	22.5	1.36x	103.12	3.87	8.8x	200	210	share and 5.2% on the oper
ern/	6/28/73	53.5	12.1	5.4	9 1/2	10.75	13.2	--	117.22	1.20	9.0x	500	300	
o.	6/ 6/74	57.4	5.7	3.0	10 1/8	12.00	18.5	1.12x	103.93	2.24	5.4x	250	610	
:ern/	11/21/73	20.0	20.8	7.0	5	7.00	40.0	--	112.14	0.08	87.5x	1,000	380	
Square Garden	6/ 6/74	28.0	5.1	1.7	5	6.75	35.0	0.96x	103.93	0.38	17.8x	250	400	
:cific/	10/14/74	--	50.0	22.7	18 3/4	29.17	55.6	--	79.42	4.51	6.5x	733	493	* Market value of $28 pri
Industries(d)	3/ 4/76	50.2	49.8	21.8	20 3/8	25.00*	22.6	.86x		2.63	9.5x	776	700	Debentures.

t for previous 16 weeks.
500 Index.
on fully diluted earnin[illegible]m continuing operations; net EPS including discont[illegible]d operations was $0.70 for [illegible] year ended 11/30/75.
itial purchase price [illegible]17 per share was adjusted to reflect a 20% stock di[illegible]d paid by Veeder on 11/15/[illegible]

UOP's Business Decline

The key argument favoring a price below $21 can be divided into three segments: first, that conditions have changed since April 1975 and that UOP's present condition, from an earnings and balance sheet standpoint, is substantially less favorable today. See Tables I and II on pages 7 and 11. Second, since Signal had no plan last April to acquire these remaining shares, their acquisition in late 1976 should be viewed independently of the first step. Finally, therefore, viewed as an independent transaction, UOP's prospects today may not merit a market premium for its shares equal to last April's premium. Table I on page 7 and Table III on the following page demonstrates UOP's recent business problems.

Table III
Summary Financial Data for UOP Inc.

I. Summary Operating Data ($MM)

Revenues		
1975	$615.0	
1974	781.0	
1973	600.8	
1972	468.2	
1971	443.3	
Pretax Profit ($ and %)		
1975	(25.7)	-
1974	35.5	4.6%
1973	25.1	4.2
1972	17.5	3.7
1971	(23.2)	-
Net Profit		
1975	$(34.9)	
1974	27.8	
1973	20.9	
1972	11.7	
1971	(29.4)	

II. Summary Balance Sheet Data ($MM)

	12/31/74	12/31/75
Cash	$25.2	$23.8
Current Assets	267.4	256.6
Notes Payable	54.5	58.5
Current Liabilities	153.3	164.7
Net Working Capital	114.1	91.9
Net Property	124.4	138.3
Other Assets	51.3	46.1
Net Assets	289.8	276.2
Long Term Debt	79.3	75.1
Other Liabilities	16.5	18.4
Net Worth	$193.9	$182.7

The Possibility of Equivalent Premiums at Offers Below $21 Per Share

As Table IV below indicates, for illustrative purposes only, that a $19 offer to current UOP shareholders provides approximately the same type of premiums in terms of market value, price, earnings multiples, and book value as did Signal's $21 offer in 1975.

Table IV

Comparison of Selected Market Ratios for Purchase of Remaining UOP Shares with Signal's Initial Purchase of UOP Shares

	1975 $21 Offer For 50.5% of UOP(a)	Alternative 1976 Offers for 49.5% of UOP		
		$17	$19	$21
Tender Price to:				
Estimated Fiscal Year EPS	9.3x	13.1x	14.6x	16.2x
Latest 12 Months EPS	8.7x	neg	neg	neg
Prior Fiscal Year EPS	7.9x	neg	neg	neg
Book Value	1.10x	1.08x	1.21x	1.34x
High Common Price for Year	1.49x	1.25x	1.39x	1.54x
Indicated Dividend	$.90	-	-	-
Indicated Yield at Tender Price	4.3%	-	-	-
Premium over Last Price	63%	39%	55%	71%

(a) Including purchase of 1,500,000 shares from UOP at $21 per share.

UOP's Stock Price May Be
Supported By Possible Signal Offer

UOP's stock price levels may currently be supported by investor speculation that Signal might make an offer to acquire the remaining stock.[a] As Table I indicates, UOP's current price of 12 1/4 is not significantly lower than the 12 7/8 level immediately prior to the first Signal offer, notwithstanding its 1975 results.

Furthermore, for the remaining shares, UOP is currently trading at 9.4x estimated 1976 earnings and 78% of book value as opposed to the prevailing 5.0-6.0x estimated 1975 earnings range and 65-70% of book value in which it traded during April 1975. These increases are difficult to ascribe solely to the general improvement in stock prices and price-earnings ratios.

Countervailing Considerations

There are, of course, a number of considerations which a UOP shareholder might raise to in order to justify

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(a) Alternatively, it should be noted controlled companies (like UOP) normally sell at a discount from the price that they would otherwise command because of concern that controlling shareholders would ignore the interests of minority shareholders and the reduced float available for institutional ownership.

at least a $21 price, the chief of which are:

1. All the considerations discussed herein which make 100% ownership of UOP attractive for Signal should compel it to pay a premium for total control of UOP in excess of the premium it offered in April 1975 for only 50.5% control. Based on UOP's closing price on June 21, 1976, a $21 offer would represent a 73% premium, compared to the 63% premium represented by the April 1975 offer of $21.

2. Recent and prospective strength in the equity market argues for a substantial premium. In a buoyant market, the premium paid should be at least as large as in a stagnant market. In the past six months, the general market, as measured by the Dow Jones Industrial Average, has appreciated 18%. The tender offer took place in a relatively depressed stock market, in which the previous six months had been flat.

B. Analysis of Alternative Methods of Acquiring UOP Shares

Effect of Alternative Offers on Signal's 1976 Earnings Per Share and Capitalization

At current UOP price levels, Signal should be prepared to pay between $90 and $120 million ($17 to $21 per share) to acquire the remaining public minority interest in UOP. Based on Signal's 1975 balance sheet and the use of approximately $38 million in cash to finance the recent purchase of its own shares, it appears that Signal may not have sufficient cash to purchase the UOP shares. Therefore, management may well have to consider either borrowing additional funds or issuing securities to UOP's shareholders as a means of obtaining 100% ownership.

We have evaluated five different methods of obtaining the remaining UOP shares - cash financed by bank borrowings, stock issued to UOP shareholders, debentures issued to UOP shareholders, and selected combinations - at varying purchase price levels.

Our recommendation, leaving aside considerations of price, is that Signal would be well advised to offer a combination of approximately equal amounts of stock and debt. While we have not had the benefit of discussions with Signal management in regard to the Company's capital needs and balance sheet objectives, we believe that Signal might become too leveraged within its "BBB/Baa" rating if all cash or debt was utilized. While we recognize that Signal's stock may currently be undervalued, and management might not want to incur the resulting earnings dilution from issuing stock, we believe that the stock market would not react favorably to an all cash or debt purchase of UOP.

Table V. on page 17 presents these alternatives and indicates the following key points:

1. An exchange involving only Signal common stock would cause estimated 1976 earnings per share dilution ranging from 3.8% to 6.1%. Alternatively, it would substantially improve Signal's balance sheet.

2. A cash offer, financed by borrowings, will improve Signal's earnings per share from 3.1% to 4.5%, but will also substantially increase its leverage. Assuming a $21 offer, Signal's net worth would be reduced from 60% to 55% of its total capitalization and short term debt would increase from 10% to 18%.

3. An offer of straight debt will not have as strong an earnings per share benefit as cash yet will result in the same reduction in net worth. See page 18 for a discussion of the benefits of using debentures in an acquisition.

4. A combination of stock plus cash or debentures will produce little or no earnings dilution and essentially enable Signal to continue its current capitalization ratios.

5. Since the first phase of Signal's acquisition was a cash transaction, the entire transaction will be subject to purchase accounting and the related goodwill charge regardless of the form the second phase takes.

Analysis of Impact on [illegible]nal [illegible] Financing the Purchase of Remaining UOP Sha[illegible]

	100% Stock			100% Cash (c)		
Total Consideration Per UOP Share	$21	$19	$17	$21	$19	$17
I. Estimated Signal 1976 EPS (e)						
Pro Forma Purchase of Own Shares	$2.91	$2.91	$2.91	$2.91	$2.91	$2.91
Pro Forma Purchase of UOP Shares (d)	2.73	2.76	2.80	3.00	3.02	3.04
% Change	(6.2%)	(5.2%)	(3.8%)	3.1%	3.8%	4.5%

II. Signal's 1975 Capitalization	Actual													
	$	%	$	%	$	%	$	%	$	%	$	%	$	%
Short Term Notes Payable (b)	$140	10.3%	$140	9.5%	$140	9.6%	$140	9.6%	$261	17.7%	$249	17.0%	$238	16.4%
Senior Long Term Debt	402	29.7	402	27.2	402	27.7	402	27.7	402	27.2	402	27.5	402	27.7
Subordinated Long Term Debt	6	.4	6	.4	6	.4	6	.4	6	.4	6	.4	6	.6
Shareholders Equity	808	59.6	929	62.9	917	62.5	906	62.4	808	54.7	808	55.1	808	55.6
Total Capitalization	$1,355	100.0%	$1,476	100.0%	$1,464	100.0%	$1,453	100.0%	$1,476	100.0%	$1,954	100.0%	$1,453	100.0%

(a) Assumes that Signal did not borrow in order to finance purchase of own shares.
(b) Includes current maturities.
(c) Assume bank borrowings at 7% and a 50% tax rate.
(d) Assumes, for comparative purposes, that acquisition of 49.5% interest in UOP will occur as of July 1, 1976.
(e) See Appendix A for the assumptions used in calculating Signal's 1976 E. P. S.
(f) Assumes a 9% coupon.

Alternative Forms of
OP Shares at Various Price Levels

	100% Debentures(f)			50% Stock, 50% Cash (c)			50% Stock, 50% Debentures		
	$21	$19	$17	$21	$19	$17	$21	$19	$17
	$2.91	$2.91	$2.91	$2.91	$2.91	$2.91	$2.91	$2.91	$2.91
	2.96	2.97	2.98	2.15	2.88	2.91	2.83	2.87	2.90
	1.7%	2.1%	2.4%	(2.1%)	(1.0%)	-	(2.7%)	(1.3%)	(.3%)

Pro Forma Acquisition of UOP ($MM) (a)

$	%	$	%	$	%	$	%	$	%	$	%	$	%	$	%	$	%
140	9.5	140	9.6	140	9.6	$201	13.6%	$195	13.3%	$189	13.0%	140	9.5	140	9.[illegible]	140	9.[illegible]
523	35.4	511	34.9	500	34.4	402	27.2	402	27.5	402	27.7	462	31.2	457	31.[illegible]	451	31.[illegible]
6	.4	6	.4	6	.4	6	.4	6	.4	6	.4	6	.4	6	.4	6	.[illegible]
808	54.7	808	55.1	808	55.6	869	58.9	862	58.9	857	59.0	869	58.9	862	58.9	857	59.[illegible]
$1,476	100.0%	$1,454	100.0%	$1,453	100.0%	$1,476	100.0%	$1,454	100.0%	$1,453	100.0%	$1,476	100.0%	$1,464	100.0%	$1,453	100.[illegible]

The Use of Debentures

The use of debentures in acquisitions, as opposed to cash supported by bank borrowings, historically has presented one major advantage: the terms, including interest rate and maturity, have often been more favorable than the issuer could have achieved in an underwritten public offering. The principal explanation for this is that the shareholders of acquired companies are often more concerned with the principal amount of the bonds being offered than with its fair makret value.

For example, under current market conditions, the likely terms for a public offering of Signal senior debt would include 20-25 year maturity and a coupon of approximately 9 3/4%. Signal, however, might probably be able to offer UOP shareholders a 25-30 year senior debenture with a coupon of 9%.

The major drawbacks with a debenture offering for Signal, of course, is the interest cost differential between 9% and the current prime rate of 7% adjusted for compensating balances. Nonetheless, if Signal management believes that short term rates are due to increase, the use of debentures would enable Signal to lock-in a non-dilutive acquisition of UOP. To the extent that Signal management might consider funding bank borrowings with a near-term issue of long term debt, it would be more prudent to offer the debentures via this acquisition.

The issues we have discussed in this memorandum are exceedingly complex and delicate. We would be pleased to have the opportunity to meet with you in Los Angeles at your convenience in order to discuss our recommendations more fully and answer any questions you may have.