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M E M O R A N D U M

TO: Our Colleagues and Clients

FROM: Samuel M. Krieger, Esq.
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DATE: November 2008

SUBJECT: **UPDATES - RULE 144(i); NEW RULE 10b-21 (SHORT SALES); RESTRUCTURINGS; REVISED FORM D**

Current financial conditions and market volatility have severely impacted on PIPES transactions and similar transactions such as reverse mergers. Nonetheless, there are a number of items of interest in the current environment.

RULE 144(i)

Revised Rule 144, including revised Rule 144(i) relating to shell companies, became effective February 15, 2008. We have had less than a year of experience and no official SEC interpretation or guidance, especially on Rule 144(i).

Rule 144(i) by its literal terms bars the sale under Rule 144 of securities issued by an issuer that was once a shell company, if at the time of sale the issuer is not a "Current Reporting Issuer." Transfer agents and issuers have been reluctant to remove legends from securities of former shell companies, notwithstanding that a non-affiliate shareholder has owned the shares for in excess of one year, and the issuer was then a Current Reporting Issuer. We understand that the SEC Staff has informally indicated that it will not object to the removal of restrictive legends from securities held by non-affiliates after all of the applicable conditions of Rule 144 are satisfied. Additionally, legends may be removed after the filing of a periodic report if the next periodic report is due more than one year after issuance of the restricted security. Presumably, if a former shell company is a "Current Reporting Issuer," transfer agents and issuers can remove legends from securities held by non-affiliates.[1]

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[1] Our firm, together with a number of other firms, recently submitted a Petition for Rulemaking regarding Rule 144(i) to the Commission. A copy of the submission is available at www.sec.gov/rules/petitions/2008/petn4-572.pdf. The proposed amendment would allow shareholders who acquired shares when an issuer was a "shell company" or former "shell company" to be able to utilize Rule 144 for a sale of unregistered securities even if the issuer has not filed its Exchange Act reports for the one year prior to the proposed sale, other than in the first year following the date the issuer ceases to be a shell company and releases "Form 10 information."

NEW RULE 10b-21

In Release 34-58774, effective October 17, 2008, the Commission permanently adopted anti-fraud Rule 10b-21 as part of its new focus on short sales. The rule, which applies only to equity securities, applies to all short sellers, including broker/dealers acting for their own accounts, who deceive specified persons about their intention or their ability to deliver securities in time for settlement, and thereafter fail to deliver securities by the settlement date. Rule 10b-21 also applies to sellers who misrepresent to broker/dealers that they own the shares being sold. The Commission believes that Rule 10b-21 will aid broker/dealers in complying with the "locate" requirements of Regulation SHO, and help reduce manipulative schemes involving "naked" short selling. The text of the rule is set forth below.

> ***Deception in connection with a seller's ability or intent to deliver securities on the date delivery is due.***
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> *PRELIMINARY NOTE to §240.10b-21: This rule is not intended to limited, or restrict, the applicability of the general antifraud provisions of the federal securities laws, such as section 120(b) of the Act and Rule 10b-5 thereunder.*
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> *(a) It shall also constitute a "manipulative or deceptive devise or contrivance" as used in Section 10(b) of this Act for any person to submit an order to sell an equity security if such persons deceives a broker or dealer, a participant of a registered clearing agency, or a purchaser about its intention or ability to deliver the security on or before the settlement date, and such person fails to deliver the security on or before the settlement date.*
>
> *(b) For purposes of this rule, the term settlement date shall mean the business day on which delivery of a security and payment of money is to be made through the facilities of a registered clearing agency in connection with the sale of a security.*
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> The Commission gave the following examples of possible Rule 10b-21 violations:
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> *If a seller deceives a broker-dealer about the validity of its locate source, the seller will be liable under Rule 10b-21 if the seller also fails to deliver securities by the date delivery is due. For example, a seller will be liable for a violation of Rule 10b-21 if it represented that it had identified a source of borrowable securities, but the seller never contacted the purported source to determine whether shares were available and could be delivered in time for settlement and the seller fails to deliver securities by settlement date. A seller will also be liable if it contacted the source and learned that the source did not have sufficient shares for timely delivery, but the seller misrepresented that the source had sufficient shares that it could deliver in time for settlement and the seller fails to deliver securities by settlement date; or, if the seller contacted the source and the source had sufficient shares that it could deliver in time for settlement, but the seller never instructed the source to deliver the shares in time for settlement and the seller otherwise refused to deliver shares on settlement date such that the sale results in a fail to deliver.*

Additionally, a seller will be liable for the violation of Rule 10b-21 for causing a broker/dealer to mark an order to sell the security as "long" if the seller knows or recklessly disregards that it is not "deemed to own" the security under Regulation SHO.

As set forth in the Preliminary Note, Rule 10b-21 is intended to supplement existing anti-fraud rules. The Commission also noted its view that a private right of action exists with respect to Rule 10b-21, and a

private plaintiff able to prove all the elements in a situation covered by Rule 10b-21 would be able to assert a claim under Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. It is unclear if the class of possible plaintiffs would include not only broker/dealers and the purchasers of the securities, but also issuers or other sellers of such securities, and may therefore open a new avenue of litigation.

RESTRUCTURINGS

Given the current market conditions, restructuring of transactions is inevitable. While the equities may be on the investor's side, there are a number of factors that should be considered to investors in terms of planning and executing restructurings, including foreclosure under the Security Agreements and involuntary bankruptcy proceedings:

1. Under Section 13 of the Securities Exchange Act of 1934, the existence of a "group" which intends to take certain specified actions with respect to an issuer must be disclosed on Schedule 13-D. Furthermore, the short swing recapture provisions of Section 16 may be attributed to sales and purchases by each member of the group. Investors should be extremely cautious that their discussions and actions with other investors do not rise to allegations that they are acting as a group requiring disclosure, and permit a possible short swing profit recapture by the issuer.

2. Investors involved in restructurings which might entail litigation, should be prepared that counterclaims and other claims, including fraud and bad faith, whether legally or factually viable, may be raised by the issuer and other affected persons resulting in delay, discovery, costs of litigation, etc.

3. Any discussion with issuers may result, even inadvertently, in the possession by the investor of "material non-public information". Appropriate written screening procedures should be implemented.

REVISED FORM D

Since September 15th, a revised Form D is in effect. Filings can now be made electronically at the election of the issuer. But beginning March 16, 2009, all issuers must file Form D electronically. The electronic filings will be easy for the public to access.

The public nature of the filings has caused the SEC to eliminate the requirement that 10% or larger shareholders must be disclosed. Form D must be filed within 15 days after the date of the first sale in the offering.

New Form D requires disclosure of the identities of all brokers and/or finders engaged in the offering of securities of an issuer under Regulation D, including FINRA CRD numbers. This might result in increased scrutiny of finders who are not registered broker-dealers, as well as provide the SEC and state regulators with new information on the activities of finders. It should be noted that states often deem persons who are compensated as "finders" to be broker-dealers, and impose rescission where alternative exemptions are not available.

The substantive changes to Regulation D, originally proposed in August 2007, are still under consideration by the Commission.

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If you have any questions regarding the matters discussed in this memorandum, please feel free to contact us.