

M E M O R A N D U M

TO: Our Clients and Colleagues

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DATE: December 2007

SUBJECT: [SEC Amendments to Rules 144 and 145- effective February 15, 2008](#)

On December 6, 2007 the SEC released the text of its recently adopted amendments to Rule 144 and Rule 145. The effective date of the amendments is February 15, 2008. The full text of the release can be found at www.sec.gov/rules/final/2007/33-8869.pdf.

In the words of the SEC, “the revised holding periods and other amendments we are adopting are applicable to securities acquired before and after the effective date of the changes announced today.”

Especially for non-affiliated investors, the amendments to Rule 144 will increase the liquidity of restricted securities -- by significantly reducing the restrictions on resales, shortening the holding periods and eliminating manner of sale requirements, such as the volume limitations which are part of the current Rule 144. In our view, it is more important than ever for transaction documents to contain valid “conversion caps” and for investors to maintain their non-affiliate status.

For issuers of restricted securities, these amendments to Rule 144 and the amended Form S-3 eligibility requirements will likely decrease the cost of capital, perhaps by reducing the liquidity discount typically imposed on such securities, but most certainly by reducing the need for issuers to agree to file and maintain the effectiveness of resale registration statements for the benefit of investors who purchase restricted securities. The costs, both in time and expenditure, of preparing, revising, amending and maintaining effective resale registration statements should be significantly reduced, if not eliminated in many cases.

The chart below sets forth in summary fashion the major provisions of revised Rule 144.

	Affiliate or Person Selling on Behalf of an Affiliate	Non-Affiliate (and Has Not Been an Affiliate During the Prior Three Months)
Restricted Securities of Reporting Issuers	<i>During six-month holding period</i> - no resales under Rule 144 permitted.	<i>During six-month holding period</i> - no resales under Rule 144 permitted.
	<i>After six-month holding period</i> - may resell in accordance with all Rule 144 requirements including: <ul style="list-style-type: none"> • Current public information, • Volume limitations, • Manner of sale requirements for equity securities, and • Filing of Form 144. 	<i>After six-month holding period but before one year</i> – unlimited public resales under Rule 144 except that the current public information requirement still applies. <i>After one-year holding period</i> - unlimited public resales under Rule 144; need not comply with any other Rule 144 requirements.
Restricted Securities of Non-Reporting Issuers	<i>During one-year holding period</i> - no resales under Rule 144 permitted.	<i>During one-year holding period</i> - no resales under Rule 144 permitted.
	<i>After one-year holding period</i> - may resell in accordance with all Rule 144 requirements, including: <ul style="list-style-type: none"> • Current public information, • Volume limitations, • Manner of sale requirements for equity securities, and • Filing of Form 144. 	<i>After one-year holding period</i> - unlimited public resales under Rule 144; need not comply with any other Rule 144 requirements.

Here are some further items of interest from the release ---

- The SEC proposal to toll the holding period for short sales and other hedging transactions was not adopted.
- “Current public information” of a reporting issuer is defined as an issuer subject to the reporting requirements of Section 13 or 15(b) of the Exchange Act for a period of at least ninety (90) days before the Rule 144 sale which has filed all required reports under section 13 or 15(d) of the Exchange Act, as applicable, during the 12 months preceding such sale (or for such shorter period that the issuer was required to file such reports), other than Form 8-K reports.
- The threshold for the filing of Form 144 by affiliates was increased to 5,000 shares or \$50,000 in a three month period.
- With respect to resale of debt securities, which includes non-participating preferred stock and asset backed securities (but not convertible securities), the manner of sale requirements have been deleted and the volume limitations have been raised to an amount that does not exceed 10% of a tranche, when added together with all sales of securities of the same tranche sold from the account of a selling security holder during a ninety (90) day period.
- The Staff noted that with respect to short sales in reliance on the safe harbor of Rule 144 which the borrower closes out using Rule 144 restricted securities, all of the conditions of Rule 144 must be met at the time of the short sale (e.g. a non-affiliate can only make the short sale after holding the relevant securities for six months).¹
- Under current Rule 144(k) shares may be sold without limitation after a two year holding period, but only by a seller who at the time of the sale is not then, and for the preceding three months has not been, an affiliate of the issuer. Rule 144(k) has now been recodified as Rule 144 (b)(1)(i) with a 6 month holding period , but the three month period for testing non-affiliate status has been retained.
- In addition to rewriting the introductory preliminary note to Rule 144, several staff positions have been codified. Most significantly, the holding periods for conversions, exchanges and cashless exercise of the warrants will tack back to the date of the original acquisition, even

¹Some recent case law involving short sales effected before an effective registration statement, with the shorts covered by shares from the effective registration statement might affect this position. However this is not the subject of this memorandum and, arguably, the SEC could take the position that Rule 144 being a “safe harbor” requires that all conditions of the Rule as promulgated be satisfied.

if the original securities did not provide for cashless exercise or conversion provided the security holder provides no consideration for the exchange other than the solely securities of the issuer. This provision will not apply, however, if the holder of the warrants has paid no consideration for the initial acquisition of warrants (example: employee stock options). The staff position on aggregation in certain pledge transactions has also been codified.

- A new Rule 144 (i) (2) governing the resale of restricted and non-restricted securities which were initially issued by a previously non-reporting shell company (as defined in Rule 405)² will be available only if the following conditions are met by the issuer :

- it has ceased to be a shell company;
- it is subject to Exchange Act reporting obligations;
- it has filed all required Exchange Act reports during the preceding twelve months; and
- at least 90 days have elapsed from the time the issuer files “Form 10 information” before any securities were sold under Rule 144.

“Form 10 information,” e.g. the “Super 8-K,” is deemed filed on the date the information is filed with the SEC, rather than the date on which the Commission deems the filing effective. This is helpful if the Staff has not finished its review of the filing or amendments responding to the staff comments.

- With respect to securities issued in business combinations, the SEC has eliminated the presumptive underwriter provision of Rule 145 with respect to registered securities acquired in a business combination transaction, except for shell companies. Rule 145(d) has been revised. Under the Rule 145 amendments, if the issuer has met the requirements of Rule 144(i)(2), non-affiliates will be able to sell their securities subject to certain provisions of Rule 144, after at least ninety (90) days have elapsed since the securities were acquired. Six months after the securities were acquired, the revised Rule 144 provisions will apply.

PRACTICE POINTERS

- Investors and their advisors should review current portfolio holdings to see which portfolio holdings have been held for more than six (6) months - and which have been held for more than 1 year - and may be sold on or at any time after the February 15th effective date of the amended Rule 144, either under the six month holding period requirements or without restriction under the one year holding period.

²A “startup company” with “a limited operating history” which Note 172 of the Release classifies as being Rule 144 eligible should be distinguished from the Rule 405 definition of a “shell company” as having “no or nominal operations.”

- Assuming that the resale of shares by the investors will not be covered by effective registration statements, it becomes even more important that there be current public information during the holding period from six months to one year. To reflect this, from the investors' perspective, we suggest that transaction documents contain covenants that the issuer will satisfy these public information requirements, with substantial penalties (similar in concept to the liquidated damages in the event of late effectiveness of a registration statement) in the event the issuer fails to do so.

- While generally, a requirement for continued listing on the OTC Bulletin Board is that the company be a reporting issuer with available current public information, "Pink Sheet" issuers only having available Form 15c-211 type information will be classified as non-reporting issuers for the purpose of Rule 144.

- In addition to conversion caps, transaction documents should require investor consent for certain transactions - e.g. voluntary redemptions - which might decrease the number of shares outstanding and cause investors to unwittingly be deemed affiliates.

- Additionally, to the extent that warrants do not currently provide for cashless exercise and there is no effective registration statement, discussions should be entered into with the issuer regarding the possibility of amending same to provide for cashless exercise by the holder. If included in a warrant, even by way of amendment (subject to certain conditions; see last A subsequent cashless exercise by the holder would allow for the holding period to be determined by the date the original warrants had been issued (or, if relevant, the later date on which all consideration from the investor had been provided). However, to maintain the commencement of the holding period to be that date, no consideration should be given by the holder for this (or any other) change in the warrant terms.

- Existing transaction documents should also be reviewed with respect to an issuer's obligation to file current public information as a reporting issuer.

- Issuers and investors should expect additional sales will occur under Rule 144 soon after the February 15th effective date. While registration rights agreements entered into with purchasers of restricted securities often require that the issuer maintain the effectiveness of a resale registration statement until the restricted securities may be resold without restriction under Rule 144(k), companies that are currently maintaining the effectiveness of, or that have agreed to file, resale registration statements for the benefit of holders of restricted securities should check the terms of any related registration rights agreements. Once the amendments to Rule 144 become effective, as a result of the shorter holding period, an issuer may no longer be obligated to keep

the resale registration statement effective, or to file a resale registration statement, if the applicable securities may be resold without restriction under revised Rule 144.

- Issuers and their counsel, as well as brokers, clearing firms and transfer agents, will need some time to revise their practices to take into account of the requirements of the amended rules. Investors should anticipate that these may vary from entity to entity and may even be revised by a particular entity over time.

- Shell companies and other filers should continue to file all reports and material required to be filed under Section 13 or 15(d) to be able to take advantage of the new rule upon consummation of a business combination.

If you have any questions or require further information, please feel free to contact our office.