

MAJOR CHANGES TO RULE 144 – SMALL BUSINESSES, REJOICE!

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On November 15, 2007, the Securities and Exchange Commission (SEC) voted unanimously to adopt several rule amendments designed primarily to enable smaller companies to raise capital more effectively and ease some of the historically burdensome reporting and disclosure requirements. In particular, the SEC adopted certain amendments to Rule 144 under the Securities Act of 1933, as amended (the Securities Act), most significantly the shortening of the minimum holding period from one year to six months for resales of “restricted securities” (securities acquired in unregistered, private sales from the issuer or an affiliate of the issuer, which is a person or entity who is controlling, controlled by or under common control with the issuer) of “reporting companies” (issuers subject to the reporting requirements of Section 13 or 15(d) of the Securities Act of 1934, as amended (the Exchange Act)).

Section 5 of the Securities Act generally requires that stock and other securities be registered with the SEC prior to their offer or sale, unless the transaction or the securities themselves are exempt from registration. Rule 144, originally adopted by the SEC in 1972, provides a safe-harbor setting forth when, and under what conditions, restricted securities may be resold into the public marketplace without registration under the Securities Act.

Prior to the 2007 amendments adopted by the SEC, in order to sell restricted securities in compliance with Rule 144, sellers were generally required to satisfy the following conditions:

- The restricted securities must have been held for at least one year;
- There must be available adequate current information regarding the issuer (i.e., the issuer must have complied with the periodic reporting requirements of the Exchange Act);
- The resale must have been within specified sales volume limitations (one could only sell in any 3-month period an amount equal to the greater of 1% of the outstanding shares of the issuer or the previous four week period’s average weekly trading volume of the issuer’s securities);
- The manner of the sales must have been routine trading transactions through brokers or market makers; and
- Notice must have been filed with the SEC on Form 144 at the time the order was placed if the sales involved more than 500 shares or an

aggregate dollar amount of greater than \$10,000 in any three month period.

Non-affiliates (persons or entities who are not controlling, controlled by or under common control with the issuer) of an issuer who held restricted securities after satisfying a two-year holding period were able to sell them under Rule 144(k) without regard to the other above-mentioned conditions, except that sales must still be made through brokers or market makers.

Under the final rule amendments, which will be effective sixty (60) days after they are published in the Federal Register, the holding period for restricted securities of reporting companies will be reduced from one year to six months. In addition, non-affiliates of reporting companies will be able to resell restricted securities freely after satisfying a six-month holding period (subject only to the Rule 144(c) public information requirement until the securities have been held for one year) and non-affiliates of non-reporting companies will be able to resell restricted securities freely after satisfying a twelve-month holding period.

For sales of restricted securities by affiliates, the SEC revised the manner of sale requirements for equity securities and eliminated them entirely for debt securities, which will allow holders of debt securities greater flexibility, including the option to privately negotiate the resale of the securities.

In addition, the requirement of filing a Form 144 was eliminated entirely for non-affiliates of an issuer, and the threshold for affiliates has been raised to being required only if the sale is for at least 5,000 shares or \$50,000.

The final amendments to Rule 144 do not incorporate the SEC's original proposal to require the holding period for restricted securities issued by reporting companies to toll, or stop, for any period in which the holder's position in the restricted securities was hedged.

The 2007 amendments to Rule 144 will have significant practical considerations for smaller companies. Under the old regime, investors in transactions such as PIPEs (private investment in public equities), which are generally used by smaller companies as a way to raise capital, would purchase their restricted securities at a discount and require the issuer to file and maintain the effectiveness of a resale registration statement for at least two years. By shortening the holding periods and reducing the manner of sale restrictions, such as the volume limitations, it is expected that (i) the discount on the sale of restricted securities and the requirement to file and maintain resale registration statements will decrease, (ii) the liquidity of restricted securities will increase, and (iii) the total cost of raising capital for issuers of restricted securities will decrease as well. This will likely increase the access to capital for smaller companies by increasing their ability to use transactions such as PIPEs.

The question remains whether the final rule amendments to Rule 144 will be retroactive, which will be known when they are published. If they will, current holders of restricted securities will obviously benefit from the shorter holding period and other changes. In addition, it is possible that small business issuers will be able to avoid costly registration obligations required in prior PIPE financings or other transactions.