

MEMO# 8692

March 6, 1997

SEC SHORTENS RULE 144 AND RULE 145 HOLDING PERIODS AND PROPOSES AMENDMENTS TO REGULATION S, RULE 144 AND RULE 145

1 Securities Act Release No. 7390, dated February 20, 1997. 2 Securities Act Release No. 7391, dated February 20, 1997. 3 Securities Act Release No. 7392, dated February 20, 1997. 1 March 6, 1997 TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 6-97 INTERNATIONAL COMMITTEE No. 10-97 SEC RULES COMMITTEE No. 26-97 RE: SEC SHORTENS RULE 144 AND RULE 145 HOLDING PERIODS AND PROPOSES AMENDMENTS TO REGULATION S, RULE 144 AND RULE 145

The Securities and Exchange Commission has adopted amendments to Rule 144 and Rule 145 under the Securities Act of 1933 to shorten the holding periods in those rules.¹ In addition, the Commission has proposed for public comment significant amendments to Rule 144 and Rule 145² and Regulation S.³ The Commission's actions are summarized below and copies of the Commission's releases are attached. Revisions to Rule 144 and Rule 145 The Commission adopted amendments to Rule 144, the non-exclusive safe harbor from registration for resales of restricted securities and securities held by affiliates of the issuer, to shorten the rule's holding periods. As amended, the holding period for resales of limited amounts of restricted securities by any person has been reduced from two years to one year and the holding period for resales by non-affiliates without compliance with the rule has been reduced from three years to two years. The revised holding periods are applicable to all securities, whether acquired before or after the effective date of the Rule 144 amendments. The Commission noted that the shorter holding periods should reduce the cost of capital, lower the illiquidity discount given by companies raising capital in private placements, and increase the usefulness of the Rule 144 safe harbor. The Commission also amended Rule 145, the rule governing the sale of securities received in connection with reclassifications, mergers, consolidations, and asset transfers. That rule has holding period requirements that correspond to the holding periods for resales in Rule 144. The Commission has revised Rule 145's holding periods to track the shortened Rule 144's holding periods. The amendments to Rule 144 and Rule 145 will become effective on April 29, 1997. Proposed Amendments to Rule 144 and Rule 145 After comprehensively reviewing Rule 144, the Commission has proposed to simplify the rule in three principal respects as well as making several other changes to the rule. First, the proposals would make it easier to determine whether a person is not an affiliate of an issuer for purposes of Rule 144 by providing a bright-line exclusion from the Rule 144 definition of affiliate. Under the proposal, a person will not be deemed to be an affiliate of an issuer if: (i) the person is

not the beneficial owner of more than 10% of any class of equity securities of the issuer; and (ii) the person is not an officer or director of the issuer; and (iii) the person is not a director of the issuer. Second, the proposal would eliminate Rule 144's manner of sale requirements, which currently require resales of securities to be made in "brokers' transactions" or in transactions with a "market maker." This change is intended to facilitate innovation in resale methods, such as the use of electronic bulletin boards. Third, the threshold requirements for filing Form 144 would increase from the current 500 shares or \$10,000 sale price test to a 1,000 shares or \$40,000 sale price test. The proposal also seeks comment on further shortening Rule 144's holding periods and eliminating the two trading volume tests that limit the amount of securities that may be resold in reliance on Rule 144, with the result that all sellers would rely on the rule's percentage of shares outstanding test. Further, the proposal seeks comment on several possible approaches to addressing the application of the Securities Act to hedging of restricted and other securities.

2The Commission also has proposed to amend Rule 145 to eliminate the provision that deems persons who were affiliates of any party to the transaction to be underwriters. The Commission notes that Rule 145 is the only rule with a presumptive underwriter provision and that it may be more appropriate to rely on Rule 144 and traditional considerations in determining whether the persons covered by Rule 145(c) are underwriters. As a corresponding change, the Commission proposes to rescind Rule 145(d) which conditionally permits these affiliates to resell securities.

Proposed Amendments to Regulation S The Commission proposed amendments to Regulation S that relate to offshore sales of equity securities of U.S. issuers and foreign issuers where the principal market for the securities is in the United States. The proposal is designed to end abusive practices in connection with offerings of equity securities purportedly made in reliance on Regulation S. The Commission states that the combination of the proposed amendments should prevent the sale of equity securities offshore under Regulation S in transactions that effectively result in unregistered distributions of the securities into the U.S. markets. Under the proposals, equity securities offered offshore by U.S. publicly traded companies and by foreign companies whose principal market for securities is in the United States would be treated as "restricted securities" within the meaning of Rule 144. This change is intended to provide purchasers of these securities with clear guidance regarding when and how these securities may be resold in the United States without registration under the Securities Act and to put purchasers on notice that resales outside of the Rule 144 safe harbor must be evaluated independently against the statutory underwriter concepts embodied in Section 2(11) of the Securities Act, regardless of the issuer's compliance with Regulation S. The Regulation S restricted period for these securities would be lengthened to two years from the 40 day period currently applicable to reporting issuers and the one year period currently applicable to non-reporting issuers. During this period, persons relying on Regulation S would not be permitted to sell these equity securities to U.S. persons (unless pursuant to registration or an exemption). In addition to lengthening the holding requirements, the Commission proposes to impose additional offering and transaction requirements on these offerings. The Commission would require: (1) issuers to include a legend on these equity securities stating that the transfer of such securities is prohibited other than in accordance with the Securities Act; (2) purchasers to certify that they are not U.S. persons and are not acquiring the securities for the account or benefit of a U.S. person, or that they are U.S. persons who purchased securities in a transaction that did not require registration under the Securities Act; (3) purchasers to agree not to engage in hedging transactions (such as short sales, and purchases and sales of put and call options) with regard to such securities unless such transactions are in accordance with the Securities Act; and (4) purchasers to agree to resell these securities only in accordance with the registration or exemptive provisions of the Securities Act or in accordance with Regulation

S. In connection with this last requirement, the Commission states its view that Regulation S does not provide any safe harbor protection for resales back to the United States by purchasers of securities placed offshore under Regulation S, particularly for equity securities of a domestic reporting issuer. Rather, such persons must determine whether they may be "underwriters" under Section 2(11) of the Securities Act and whether an exemption from registration for resales is available. In addition, the proposal would prohibit the use of promissory notes as payment for these securities. The Commission asks if the restricted period should be shorter than two years. In addition, the Commission seeks comment on all of the proposed changes and particularly asks if any or all of the proposed changes obviate the need for the longer restricted period. The Commission also proposed to eliminate the current requirement that issuers of Regulation S securities report those sales on Form 8-K. Instead, issuers would be required to report those sales quarterly. In addition, the Commission proposed in new Rule 905 to make explicit that when restricted equity securities of any domestic issuer or of a foreign issuer where the principal market for the equity securities is in the United States are resold offshore under Regulation S, such securities will retain their status as restricted securities after the resale. Comments on the proposals regarding Regulation S, Rule 144, and Rule 145 must be provided to the Commission by April 29, 1997. Accordingly, please provide me with any comments you have on the proposals no later than April 2, 1997. You can reach me by phone at 202/326-5821, e-mail at donohue@ici.org or by fax at 202/326-5827. Dorothy M. Donohue
Assistant Counsel Attachments (in .pdf format)

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