SEC Adopts Amendments to Rules 144 and 145

The Securities and Exchange Commission has adopted several significant amendments to Rules 144 and 145 under the Securities Act of 1933. While the SEC's stated objective was to enhance capital-raising opportunities for smaller companies, the revised rules have significant implications for all public companies and their stockholders. The revised rules will also affect resales of registered securities received by affiliates of the target company in a merger.

Rule Changes

The following are the highlights of the SEC actions:

- *Shorter Holding Periods.* The SEC shortened the holding period for restricted securities issued by reporting companies from one year to six months. The current one-year holding period for restricted securities of non-reporting companies will remain in place.

- *Non-affiliate Compliance.* Once the six-month holding period has been met, non-affiliates of reporting companies may freely resell restricted securities provided that the public information requirements of Rule 144(c) are met. The manner of sale and volume limitations have been eliminated, and the current public information condition remains only until the securities have been held for one year. The SEC also eliminated the requirement for non-affiliate sellers to file Form 144.

- *Affiliate Compliance.* Affiliates of reporting companies will still need to comply with manner of sale and volume requirements for resales of both restricted and unrestricted securities.

- *Thresholds.* The thresholds applicable to Form 144 filing requirements have been increased to sales that exceed 5,000 shares or $50,000 within a three-month period.

- *Debt Securities.* The SEC relaxed the Rule 144(e) volume limitations for debt securities by adding an alternative test that would permit resale of up to 10% of a tranche in any three-month period. The SEC also eliminated manner of sale requirements for sales of debt securities by affiliates.

- *Rejection of Tolling For Hedging Activities.* The SEC did not adopt the portion of the proposal that would have suspended any Rule 144 holding period for up to six months while the security holder of reporting company restricted securities hedged those securities. After receiving many public comments against this aspect of the proposal, and noting the lack of any strong evidence that hedging resulted in Rule 144 abuses, the SEC acknowledged that any such provision would unduly complicate Rule 144 and create significant monitoring costs.

- *Elimination of 145 "Presumptive Underwriter" Doctrine.* The amendments to Rule 145 eliminate the presumptive underwriter doctrine (except with respect to transactions involving shell companies) and revise the resale provisions of Rule 145(d) to conform them to the Rule 144 changes. Thus, target affiliates will no longer be restricted in their resales of registered shares following a merger.

The amendments become effective in early February 2008.

Consequences

In light of these amendments, we think the following consequences are likely:

- revisions to standard Rule 144 representation letters to reflect the less onerous requirements;

- increased market share for "144A for life" offerings with narrower credit spreads as compared to 144A offerings with registration rights;

- emergence of PIPEs without registration rights, at either higher discounts or with more warrant coverage;

- little change in rights demanded by venture capitalists in private company financings, although some modifications in the specific registration rights provisions;

- increased use of unregistered stock in acquisitions; and

- the demise of affiliate letters in public company M&A transactions with stock consideration.

We recommend that issuers with outstanding resale registration statements and registration rights agreements review the underlying contracts to determine what impact the new rules might have.

Contact Information

If you would like to learn more about these amendments and their implications, please contact your usual legal advisor at Ropes & Gray.