

November 19, 2007

## SEC Amends Rules 144 and 145 and the Disclosure and Reporting Requirements for Smaller Companies; Creates New Exemptions From Registration for Employee Stock Options

On November 15, 2007, the SEC approved a series of noteworthy amendments to Rules 144 and 145 and the disclosure and reporting requirements for smaller companies. The SEC also adopted two exemptions from Exchange Act registration requirements for compensatory stock options. Among the most important of these changes are:

- the liberalization of the regime governing the resale of restricted securities under Rule 144, including the shortening of holding periods and the removal of most requirements for resales by non-affiliates of restricted securities (note that in response to commenters' concerns that monitoring hedging activity would unduly complicate compliance with Rule 144, the SEC elected not to adopt proposed tolling provisions that would have tolled securityholders' holding periods upon entry into certain hedging transactions);
- the elimination of Rule 145's presumptive underwriter provision except for transactions involving shell companies and the revision of Rule 145(d)'s resale restrictions to conform to certain of the changes to Rule 144;
- the reduction of disclosure obligations for a broader group of smaller companies; and
- the creation of new exemptions from registration under Section 12(g) of the Exchange Act for compensatory employee stock options issued by both reporting and non-reporting companies;

The exemptions from Section 12(g) will become effective immediately. The changes relating to smaller reporting companies will become effective 30 days after publication in the *Federal Register*. The amendments to Rule 144 and Rule 145 will become effective 60 days after publication in the *Federal Register*.

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**I. Rule 144**

The SEC adopted a number of significant amendments to Rule 144:

- The Rule 144(d) holding period for resales of restricted securities has been shortened from one year to six months, where the issuer is subject to Exchange Act reporting obligations for at least 90 days before the sale of the restricted securities.
- Non-affiliate holders of restricted securities of a reporting company may therefore resell freely after meeting the six-month holding period, so long as current information regarding the issuer is publicly available, as required by Rule 144(c), and such holders have not been affiliates of the reporting company for at least three months before the sale.
- Holders of restricted securities of non-reporting companies continue to be required to hold their securities for one year before any public resale, but non-affiliates may freely resell after the one-year holding period is met.
- Non-affiliate holders of restricted securities of any reporting company may resell freely after meeting a one year holding period, regardless of the current reporting by the company.
- The manner of sale requirements set forth in Rule 144(f) with respect to affiliate resales of debt securities have been eliminated.
- Volume limitations with respect to affiliate resales of debt securities have been relaxed by adding an alternate determination of volume limitations for debt securities to Rule 144(e) (this was not included in the original proposal). Under the alternative volume limitation test, resales of debt securities in amounts up to 10% of that tranche of securities are permitted in a three month period.
- The Form 144 filing requirement in Rule 144(h) has been amended to raise the number of share and aggregate sale price thresholds for such filing to the greater of 5,000 shares (rather than the initially proposed 1,000 shares) or \$50,000 within a three-month period and impose the filing requirement only on affiliates of the issuer.

The SEC did not adopt certain proposed amendments to Rule 144:

- The proposed tolling provision that would have tolled the holding period for restricted securities under Rule 144(d) while a securityholder has a short position or has entered into a put equivalent position with respect to the restricted security was not adopted. The SEC cited concerns raised by commenters that monitoring hedging activity with regard to restricted securities would make compliance with Rule 144 very difficult.
- The SEC determined that the proposals related to the coordination of Form 144 filing requirements under Rule 144(h) with Form 4 filing requirements under Section 16(a) of the Exchange Act require further consideration, particularly on technical aspects of the integration. The SEC will continue to solicit comment on this topic.

## II. Rule 145

The SEC has adopted an amendment eliminating Rule 145's presumed underwriter provisions except for transactions involving blank check or shell companies. Under the amendment, only a party to a Rule 145(a) business combination transaction involving shell companies (other than business combination related shell companies) and such party's affiliates will be presumed an underwriter subject to the resale restrictions of Rule 145(d). The SEC also approved changes to the Rule 145(d) resale restrictions to conform such restrictions to certain of the amendments to Rule 144 discussed above.

## III. Smaller Reporting Companies

The SEC has adopted amendments to its disclosure and reporting regimes under both the Securities Act and the Exchange Act to increase the number of companies that are eligible to comply with the scaled disclosure and reporting requirements currently in place for small business issuers. The amendments create a new category of issuers called "smaller reporting companies," which includes most companies with a public float below \$75 million. In addition, the amendments eliminate Regulation S-B and the associated forms currently used by small business issuers and integrate the provisions of Regulation S-B into Regulation S-K and Regulation S-X. Current S-B filers would have the option to continue using the S-B forms for periodic reports until they file their next annual report on Form 10-KSB or Form 10-K.

## IV. Section 12(g) of the Exchange Act

Pre-IPO companies with large pools of optionholders have faced the possibility of having to register under Section 12(g) of the Exchange Act as a result of having more than 500 optionholders. After having provided relief on an *ad hoc* basis through no-action letters, the SEC has now adopted two new exemptions from registration under Section 12(g) of the Exchange Act for compensatory employee stock options.

Under the new rules, non-reporting companies will be eligible for an exemption from registration of compensatory employee stock options issued under a written compensatory stock option plan as long as (a) eligible option holders are limited to employees, directors, consultants, and advisors, (b) transferability of the options and the shares received on exercise of the options is restricted, and (c) option holders and holders of the shares received on exercise of the options receive the same risk factor and financial information that is of the type that would be required under Rule 701 under the Securities Act if securities sold in reliance on Rule 701 exceeded \$5 million in any 12 month period.

In addition, the SEC has adopted a separate exemption for compensatory employee stock options of reporting companies that are required to file reports under the Exchange Act pursuant to Section 13 or Section 15(d) thereof, as option holders would have access to the company's publicly filed Exchange Act reports. In each case, the exemption only applies to the company's compensatory stock options and does not extend to the class of stock underlying the options.

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The foregoing is based on oral discussions at the SEC's open meeting, the SEC's press release announcing the results of the open meeting, and the SEC's summary statements on the matters, and the specific language of the SEC rules, and guidance will not be known until the relevant releases are published. We expect to provide a more detailed description and analysis of the new rule amendments promptly after the releases are published.

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