SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 230 and 239

[Release No. 33–7391; File No. S7–07–97]

RIN 3235–AH13

Revision of Rule 144, Rule 145 and Form 144

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rules.

SUMMARY: The Commission proposes changes to make Rule 144, a safe harbor from the Securities Act definition of the term ''underwriter,'' easier to understand and apply. The proposed amendments would revise the Preliminary Note to Rule 144 to restate the intent and effect of the rule, add a bright-line test to the Rule 144 definition of ''affiliate,'' eliminate the Rule 144 manner of sale requirements, increase the Form 144 filing thresholds, include in the definition of ''restricted securities'' securities issued pursuant to the Securities Act Section 4(6) exemption, clarify the holding period determination for securities acquired in certain exchanges with the issuer and in holding company formations, and streamline and simplify several rule provisions. The Commission also proposes to eliminate the presumptive underwriter provisions of Rule 145. Additionally, the release solicits comment on changes to the Rule 144 holding periods that differ from those being adopted today in a companion release, elimination of the trading volume tests to determine the amount of securities that can be resold under Rule 144, and several possible regulatory approaches with respect to certain hedging activities.

DATES: Comments should be received on or before April 29, 1997.

ADDRESSES: Comments should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. Comments also may be submitted electronically at the following E-mail address: rule-comments @ sec.gov. All comment letters should refer to File No. S7–07–97; this file number should be included in the subject line if E-mail is used. Comment letters will be available for inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549. Electronically submitted comment letters will be posted on the Commission's Internet Web Site (http://www.sec.gov).

FOR FURTHER INFORMATION CONTACT: Elizabeth M. Murphy, Mark W. Green or Michael Hyatte, Office of Chief Counsel, Division of Corporation Finance, at (202) 942–2900, 450 Fifth Street, N.W., Washington, D.C. 20549.

SUPPLEMENTARY INFORMATION: The Commission is proposing amendments to Rule 144,[1] Rule 145[2] and Form 144[3] under the Securities Act of 1933 (''Securities Act'').[4]

I. Executive Summary

Securities Act Rule 144 provides a safe harbor for the resale of restricted and control securities.[5] The rule permits persons who hold such securities to publicly sell them without registration and without being deemed underwriters, if certain conditions are satisfied. When Rule 144 was adopted in 1972, the Commission noted that it was experimental in nature and would be rescinded or amended, as necessary, based on actual experience.[6] Since its adoption, the Commission has monitored the operation of Rule 144 and has eliminated many compliance burdens where consistent with the investor protection objectives of the Securities Act.

The Commission is continuing its efforts to improve the clarity and usefulness of Rule 144 and to eliminate unnecessary compliance burdens. In June 1995, the Commission proposed to permit limited resales of restricted securities after a one-, rather than two-year holding period, and to allow unlimited resales of such securities by non-affiliates after a two-, rather than three-year holding period (''1995 Release'').[7] The proposed new holding periods are being adopted in a companion release being published today (''Adopting Release'').[8]

After reviewing the comments received on the 1995 Release, the Commission staff undertook a more comprehensive review of Rule 144 to determine whether other provisions of the rule were unnecessarily restrictive or in need of updating. This Release proposes several revisions intended to make Rule 144 easier to understand and apply.

The proposals in this release would reorganize and rewrite the text of Rule 144, including the Preliminary Note, in a more succinct and straightforward fashion. The proposals also would simplify and update the rule in three main ways.[9]

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. Pursuant to the proposal, all persons not subject to the provisions of Section 16[10] of the Securities Exchange Act of 1934 (''Exchange Act'')[11] would be deemed not to be affiliates of an issuer for purposes of Rule 144.

Second, the proposals would eliminate the manner of sale requirements. [12] This would facilitate innovation in the methods used to resell restricted securities, 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.

Additionally, this Release solicits comment on other possible changes to Rule 144, including:

- Further revisions to the Rule 144 holding periods that would result in changes to either the one-or two-year holding periods being adopted today, or both;
- Elimination of the two trading volume tests that limit the amount of securities that may be sold in reliance on Rule 144, with the result that all sellers would rely on the percentage of shares outstanding test; and
- Several possible approaches to addressing the application of the Securities Act to hedging of restricted and other securities.

Finally, the Commission is proposing to amend Securities Act Rule 145, a Securities Act rule relating to certain significant transactions, such as mergers, to eliminate the resale limitations that are based on a ''presumptive underwriter'' approach.

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[1] 17 CFR 230.144.

[2] 17 CFR 230.145.

[3] 17 CFR 239.144.

[4] 15 U.S.C. 77a *et seq.*

[5] Restricted securities generally are securities issued in non-public offerings; control securities are securities owned by affiliates of the issuer.

[6] Release No. 33–5223 (January 11, 1972) [37 FR 591].

[7] Release No. 33–7187 (June 27, 1995) [60 FR 35645]. Additionally, the Commission requested comment on whether Rule 144 should be revised to address new trading strategies such as equity swaps. Comment letters on the 1995 Release are available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549. Interested persons should refer to File No. S7–17–95.

[8] Release No. 33–7390 (February 20, 1997).

[9] In addition, the Commission proposes to codify existing staff positions regarding determination of the holding period for securities acquired solely in exchange for other securities of the same issuer and in holding company formations, as well as the treatment of securities issued pursuant to the exemption under Section 4(6) of the Securities Act [15 U.S.C. 77(d)(6)] as restricted securities.

[10] 15 U.S.C. 78p.

[11] 15 U.S.C. 78a *et seq.*

[12] The manner of sale requirements are contained in current Rule 144(f) [17 CFR 230.144(f)]. Current Rule 144(g) [17 CFR 230.144(g)], which defines the term ''brokers' transactions'' for purposes of Rule 144, also would be rescinded.

Instead, persons who receive securities in these transactions would be treated the same as other purchasers of securities.

II. Background

The Securities Act protects investors primarily by requiring public information about issuers to be available to investors and potential investors at the time they make decisions regarding investment in an issuer's securities. The statute thus prohibits offerings unless the securities being offered are registered with the Commission or an exemption from registration is available.

The Securities Act requires registration not only of direct distributions of securities by issuers to the public, but also indirect distributions involving the transfer of unregistered securities from issuers or affiliates to persons in non-public transactions followed by large-scale public transfers of the securities by such persons. To regulate these types of indirect distributions, the Securities Act, under certain circumstances, treats even individual investors who are not securities professionals as underwriters if they act as links in the chain through which securities move from issuers to the public.

The term ''underwriter'' is defined in Section 2(11) of the Securities Act [13] to mean ''any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking.'' [14] The definition of underwriter is relevant to the ''ordinary trading'' exemption provided in Section 4(1) of the Securities Act, [15] which states that the registration provisions shall not apply to transactions by any person other than an issuer, underwriter or dealer. [16]

The statutory definition of underwriter does not provide a means to determine objectively whether a person purchased securities from the issuer or an affiliate with a view to distribution of the securities. Rule 144 was adopted as a non-exclusive safe harbor to set forth objective criteria that could be relied on by persons who wanted to resell restricted or control securities, but who were concerned whether they could be deemed to be engaged in a distribution, and therefore deemed to be underwriters under Section 2(11). The rule provides that a person who complies with its terms and conditions will not be engaged in a distribution of securities and, thus, not be an ''underwriter'' within the meaning of Section 2(11) of the Securities Act.

III. Discussion of Proposals

A. Changes to the Preliminary Note to Rule 144

The Preliminary Note to Rule 144 would be revised to better describe the two types of common transactions that raise questions as to whether a person who sells securities is acting as an underwriter (the resale of restricted securities and the resale of securities, whether or not restricted, by or on behalf of an affiliate of the issuer). It also explains that satisfaction of the criteria of Rule 144 will cause the sale of restricted or control securities to be viewed as an ordinary trading transaction rather than a ''distribution'' of such securities that would require registration under the Act.

The proposed Note states explicitly that if a sale of securities is made in accordance with all of the applicable provisions of Rule 144: (1) any person who sells restricted securities will be deemed not to be an underwriter for that transaction; (2) any person who sells restricted or other securities on behalf of an affiliate of the issuer will be deemed not to be an underwriter for that transaction; and (3) the purchaser receives unrestricted securities. The proposed Note also incorporates the statement in current Rule 144(j) [17] that Rule 144 is not an exclusive safe harbor and therefore does not eliminate or otherwise affect the availability of any other exemption for resales under the Securities Act.

Are there other matters that should be discussed in the Preliminary Note? Are there matters discussed in the Preliminary Note that should be removed?

B. Change to the Rule 144 Definition of ''Affiliate''

Rule 144 defines an affiliate of an issuer as a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, such issuer.[18] This subjective ''facts and circumstances'' test presents a great deal of uncertainty regarding whether a seller is an affiliate of the issuer and introduces additional regulatory complexity that is not always necessary. Issuers and sellers of securities have, therefore, asked for greater guidance in determining who is an affiliate.

Under the proposal, the same criteria used to determine those persons that are not ''insiders'' under Exchange Act Section 16 would be used for Rule 144. Many practitioners already use the Section 16 criteria as a guide. The Commission believes it is likely that most persons who are not officers, directors or 10% holders are not in a ''control'' position.[19] Therefore, the Commission proposes to add the following to the definition of affiliate in Rule 144.

A person shall be deemed not to be an affiliate for purposes of this section if the person: (i) is not the beneficial owner, directly or indirectly, of more than 10% of any class of equity securities of the issuer; (ii) is not an officer of the issuer; and (iii) is not a director of the issuer.

A note would add:

The determination of a person's beneficial ownership and whether that person is an ''officer'' shall be made in accordance with Rule 16a–1 [20] of this chapter, regardless of whether the issuer's securities are subject to Section 16 of the Securities Exchange Act of 1934 (''Exchange Act'') and regardless of whether the class of securities is registered under Section 12 of the Exchange Act.[21]

The proposal clearly excludes from the definition persons who are not executive officers, directors or 10% holders. Members of one or more of these classes may contend, nevertheless, that they are not affiliates because they are not in a ''control'' position. For such persons, the determination of affiliate status would be a ''facts and circumstances'' test.

The need for increased certainty in the definition of affiliate also was recognized by the Advisory Committee on the Capital Formation and Regulatory Processes (''Advisory Committee''). The Advisory Committee recommended an objective test for

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[13] 15 U.S.C. 77(b)(11).

[14] Section 2(11) states that the term ''underwriter'' shall not include a person whose interest is limited to taking a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commission, and uses the term ''issuer'' to include, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer.

[15] 15 U.S.C. 77(d)(1).

[16] Sections 4(3) and 4(4) of the Securities Act [15 U.S.C. 77(d)(3) and (d)(4)] provide exemptions from the registration requirements for transactions by dealers and brokers not acting as underwriters.

[17] 17 CFR 230.144(j).

[18] Rule 144(a)(1) [17 CFR 230.144(a)(1)].

[19] Unlike Section 16, the Rule 144 safe harbor would ignore whether the company has equity securities registered under Section 12 of the Exchange Act.

[20] 17 CFR 240.16a–1. The definitions of the terms ''beneficial owner'' and ''officer'' in Rule 16a–1 would be used whether or not the securities to be resold in reliance upon the Rule 144 safe harbor are equity securities registered under Section 12 of the Exchange Act.

[21] Proposed Rule 144(a)(1).

determining affiliate status as part of an overall reform package that includes registration of most securities that, under the current system, would not be registered.[22] The Advisory Committee definition would include only the following persons as affiliates: the Chief Executive Officer; inside directors; holders of 20% of the company's voting power; and holders of 10% of the voting power with at least one director representative on the board.[23] Should this definition be adopted, instead of the one proposed, even in the absence of the other reforms recommended by the Advisory Committee?

Is there a need to provide more objective guidance as to who is an affiliate for purposes of Rule 144? Is reliance on the Section 16 insider test over-inclusive or under-inclusive? Should the exclusion from the definition of affiliate include an express presumption that those persons not so excluded are affiliates? If so, should such a presumption be rebuttable?

For affiliate status based on shareholdings, is the 10% test appropriate, or should it be higher (such as 20%), or lower (such as 5%)? Should the shareholdings test be combined, at a certain level of ownership, with the ability to place persons on the board of directors? For example, as recommended by the Advisory Committee, should the safe harbor exclude only those 10% holders that also have the ability to place at least one director on the board?

Should the definition of affiliate exclude non-employee directors? Should non-employee directors be excluded from the definition only if they have less than a specified amount of shareholdings, such as 2%, 3% or 5%? If non-employee directors should be excluded from the definition of affiliate, should the exclusion apply to non-employee directors who are securities professionals? Should the exclusion apply to non-employee directors who are representatives of controlling shareholders?

Some have argued in favor of retaining a subjective test, given the varied contractual arrangements with a control feature entered into by issuers, particularly smaller companies. Should a facts and circumstances test be retained in order to reflect the different ways a control relationship can be established with an issuer?

[22] *See Report of the Advisory Committee on the Capital Formation and Regulatory Processes* (July 24, 1996) (the ''Advisory Committee Report'') at p. 24.

[23] *See Advisory Committee Report* at p.24.

C. Manner of Sale Requirements

Rule 144(f) requires that securities be sold in ''brokers' transactions,'' [24] or in transactions directly with a ''market maker,'' as that term is defined in Section 3(a)(38) of the Exchange Act.[25] Additionally, the rule prohibits a seller from: (1) soliciting or arranging for the solicitation of orders to buy the securities in anticipation of, or in connection with, the Rule 144 transaction; or (2) making any payment in connection with the offer or sale of the securities to any person other than the broker who executes the order to sell the securities. These manner of sale restrictions do not apply to securities sold for the account of a non-affiliate of an issuer when the holding period of Rule 144(k) is met.[26]

The manner of sale requirements were intended to assure that special selling efforts and compensation arrangements usually associated with a distribution are not present in a Rule 144 sale.[27] The manner of sale requirements currently, however, appear to impose obstacles to transactions that are not distributive in nature. For example, a consequence of the manner of sale requirements is that a seller may not privately negotiate a sale of a public company's stock in reliance on Rule 144 without a broker even if the seller does not solicit the buyer's purchase of the securities, the holding period has been satisfied and the amount sold is within the volume limitations. Similarly, sellers are unable to use trading systems such as passive bulletin boards to contact potential buyers that have indicated an interest in buying the type of securities to be sold under Rule 144.[28]

When a transaction is made in accordance with the current public information, holding period, volume and notice requirements of Rule 144, the manner in which that transaction is effected does not appear to be determinative of a distribution. Therefore, it appears that the manner of sale requirements of Rule 144(f) are not necessary to satisfy the purpose of Rule 144 and are proposed to be eliminated.[29]

Removal of the manner of sale requirements would permit holders of restricted securities to solicit purchasers in a Rule 144 transaction.[30] Is it consistent with the Rule's ''non-distribution'' purpose to allow either transactions in which special selling efforts may be used or privately negotiated transactions? Should the manner of sale requirements be retained but modified to permit specific types of transactions other than brokers' and market makers' transactions, *e.g.*, passive bulletin board transactions?

Are there other purposes served by the manner of sale requirements that would justify retaining those requirements? For example, does the manner of sale requirement serve an important purpose by inserting a market professional as a ''gatekeeper'' that assures compliance with the public information, holding period, volume, and notice requirements of the rule? How will the removal of the manner of sale requirements affect participants, such as transfer agents, brokers and market makers, in Rule 144 transactions? Will transfer agents assume a greater role in determining compliance with the resale provisions?

Would the elimination of the definition of ''brokers' transactions'' in Rule 144(g) affect the ability of brokers to determine compliance with the exemption provided by Securities Act Section 4(4)? Would removal of the manner of sale requirements diminish security transaction transparency by encouraging more privately negotiated transactions? If so, would the markets be adversely affected, particularly for stocks of smaller companies and more thinly traded securities?

D. Notice of Sale Requirement

Rule 144(h) requires a person selling more than 500 shares or $10,000 of securities in reliance on the rule during any three-month period to file a notice on Form 144 with the Commission. The Report of the Commission's Task Force

[24] Current Rule 144(g) defines the term for purposes of Rule 144.

[25] 15 U.S.C. 78c(a)(38).

[26] The manner of sale requirements also do not apply to securities sold for the account of the estate of a deceased person or for the account of a beneficiary of such estate, provided the estate or beneficiary is not an affiliate of the issuer.

[27] Release No. 33–5186 (September 10, 1971) [36 FR 18586].

[28] The use of electronic bulletin boards has been the subject of recent no-action letters. *See Real Goods Trading Corp.* (June 24, 1996), *PerfectData Corp.* (August 5, 1996) and *The Flamemaster Corp.* (October 29, 1996).

[29] If this proposal is adopted, Form 144 also would be amended to eliminate references to the manner of sale requirements. Rule 144(g) defines the term ''brokers' transactions'' for purposes of Rule 144. It would also be deleted if Rule 144(f) is eliminated.

[30] Elimination of the manner of sale requirements effectively would treat resales complying with the public information, holding period, volume, and notice requirements of the rule as not constituting a ''distribution'' for Securities Act purposes. The Commission notes, however, that such resales under certain circumstances would be subject to the requirements of recently adopted Regulation M. 17 CFR 242.100 *et seq.* Regulation M was adopted in Release No. 34–38067 (December 20, 1996) [62 FR 520].

on Disclosure Simplification (''Task Force Report'')[31] recommended that the thresholds for small business issuers be raised to 500 shares or $40,000, and that the thresholds be raised to 1,000 shares or $100,000 for other issuers.

The $10,000 limit was established in 1972. This amount, adjusted for inflation, is approximately $36,000 today. The Commission therefore believes that it is appropriate to increase the $10,000 threshold. Under the proposed requirements, Form 144 would be filed if the amount of securities to be resold in reliance upon Rule 144 during any three-month period exceeds 1,000 shares or has an aggregate sales price in excess of $40,000.

Should the share number and dollar thresholds be set at a different combination of share number and dollar amount, *e.g.*, any share number ranging between 500 and 2,000 shares and any dollar amount ranging between $10,000 and $100,000 for sales of securities of all types of issuers? Should there be a single filing threshold, and if so, which threshold should be retained, the share number or dollar amount threshold? If there were a single threshold based on share number, would 500 shares, 1,000 shares or a different share number ranging between 500 and 2,000 shares be appropriate? If there were a single threshold based on dollar amount, would a different dollar value ranging between $10,000 and $100,000 be appropriate?

The Commission is not proposing to establish different filing thresholds for sales of small business issuer securities out of concern that different standards for small business issuers and other issuers would needlessly complicate the Form 144 requirements. Should the Commission establish separate thresholds for small business and non-small business issuers, and if so, are the thresholds recommended in the Task Force Report appropriate? The Commission notes that a smaller threshold for small businesses would result in more filings by persons selling small business securities. This could be justified in that a smaller transaction can have a greater impact on a small business issuer.

E. Other Proposed Amendments to Rule 144

1. Codification of Staff Interpretive Positions

The Commission is proposing to codify a variety of staff interpretive positions regarding Rule 144 in order to make it easier to comply with the rule.

a. Holding Period—Conversions and Exchanges

First, the Commission proposes to amend the Rule 144 provision on calculating the holding period for securities acquired upon conversion of other securities of the same issuer. Rule 144 generally allows holders to count the time they held securities surrendered for conversion or exchange when counting the holding period for the securities received in the conversion or exchange, what is commonly referred to as ''tacking'' the holding periods.[32] This provision of Rule 144 does not state, however, whether the surrendered securities must have been convertible by their terms in order for tacking to be permitted. This silence has led to confusion by some persons regarding how to calculate their Rule 144 holding period.

Rule 144 permits tacking of holding periods in the case of securities received in a conversion because the exchange continues the shareholder's investment in that *same* issuer. Because the significant factor in this analysis is that securities of the issuer are exchanged for other securities of that issuer, the staff has taken the interpretive position that tacking is allowed whether or not the surrendered securities are convertible by their terms. The proposed amendment would clarify the application of this provision by codifying the staff's interpretive position.[33]

b. Holding Period—Holding Company Formations

Second, the proposed revisions would codify a staff position to clarify that holders can tack the Rule 144 holding period in connection with transactions effected solely for the purpose of forming a holding company.[34] Although tacking through a holding company formation appears to be contemplated by the rule, the rule does not clearly state when and how this is allowed.[35] The proposed revisions would codify a staff interpretive position by allowing for tacking in holding company formations, subject to the following conditions:

- The holding company's securities must be issued in a transaction involving an exchange of securities as part of a reorganization of the predecessor into a holding company structure;
- Holders must receive securities of the same class evidencing the same proportional interest in the holding company as they held in the predecessor; and
- Immediately following the transaction, the holding company must have no significant assets other than securities of the predecessor and its existing subsidiaries and have substantially the same assets and liabilities on a consolidated basis as the predecessor had prior to the transaction.[36]

c. Definition of Restricted Securities

Third, the proposed revisions would codify the staff position that securities acquired from the issuer pursuant to the exemption under Section 4(6) of the Securities Act should be considered ''restricted securities.''[37] Section 4(6) provides an exemption for non-public offerings of less than $5 million that are made only to accredited investors.[38] Because the resale status of securities received in Section 4(6)-exempt transactions should be the same as securities received in other non-public offerings, the staff has taken the interpretive position that securities sold pursuant to the Section 4(6) exemption also should be deemed to be restricted securities.[39]

2. Simplification and Streamlining

The Commission is proposing a number of revisions intended to make Rule 144 more readable and easily understood. The simplifying revisions would address the conditions to be met to satisfy the rule, the current public information requirement, the volume limitations and the holding period provisions relating to trusts and estates in addition to the proposed revisions to the Preliminary Note to Rule 144 discussed above. Current paragraph (k),[40] which applies to restricted securities held by non-affiliates for more

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[31] The Task Force Report was issued in March 1996. The recommendations concerning Rule 144(h) are discussed on p. 71.

[32] Rule 144(d)(3)(ii).

[33] Proposed Rule 144(d)(3)(ii). This would codify the position taken in *Planning Research Corporation* (November 6, 1980). The provision also would state that if securities are acquired from the issuer solely in exchange (in addition to upon conversion) for other securities of the issuer, the securities so acquired are deemed to have been acquired at the same time as the securities surrendered in the exchange. This also would codify a staff interpretive position.

[34] Proposed Rule 144(d)(3)(ix).

[35] Rule 144(d)(3)(viii) [17 CFR 230.144(d)(3)(viii)].

[36] *Morgan Olmstead* (January 8, 1988).

[37] Proposed Rule 144(a)(3)(vi).

[38] The Section 4(6) exemption also requires the filing of a notice of the offering with the Commission. This notice currently is filed on Form D. In Release No. 33–7301 (June 14, 1996) [61 FR 30405], the Commission proposed to eliminate the Form D filing requirement.

[39] In Release No. 33–7392 (February 20, 1997) concerning Regulation S (''Regulation S Proposing Release''), the Commission is proposing to revise Rule 144(a)(3) [17 CFR 230.144(a)(3)] to define equity securities of domestic issuers, and of foreign issuers where the principal market for such securities is in the United States, issued pursuant to Rule 901 or 903, as restricted securities.

[40] 17 CFR 230.144(k).

than two years, would be simplified and re-designated as paragraph (g).

Current paragraph (i)[41] requires the person filing a Form 144 to have a bona fide intention to sell the securities described in the Form 144 within a reasonable period of time after that filing. The wording of this requirement is proposed to be simplified and moved into the Form 144 filing requirement.[42]

Finally, current paragraph (j),[43] which states that Rule 144 is a non-exclusive provision that does not affect the availability of any Securities Act exemption from registration for resales of securities, would be eliminated. As discussed above, the non-exclusive nature of Rule 144 is proposed to be discussed in the Preliminary Note. This would be consistent with other Commission safe harbor provisions.[44]

F. Rule 145

Securities Act Rule 145 provides that exchanges of securities in connection with reclassifications of securities, mergers or consolidations or transfers of assets that are subject to a shareholder vote constitute sales of those securities. As a result, unless an exemption is available, the offering of securities in those transactions must be registered under the Securities Act.

The rule explicitly deems persons who were affiliates of any party to the transaction to be underwriters.[45] Therefore, the Section 4(1) resale exemption is not available to these persons for resales of securities acquired in connection with transactions described in the rule. The rule provides some relief from this ''presumptive underwriter'' provision, however, by permitting the affiliates to resell securities received in the transaction in compliance with the holding period and other requirements of Rule 145(d).[46]

Rule 145 is the only Securities Act rule that contains a presumptive underwriter provision. The Commission believes that it may no longer be appropriate to rely on a presumptive underwriter approach when addressing the resales of securities acquired in Rule 145 transactions. Rather, it appears to be more appropriate to rely on the provisions of Rule 144 and traditional considerations in determining whether the persons covered by current Rule 145(c) are underwriters in connection with resales. The presumptive underwriter and resale provisions of Rule 145(c) and (d) are, therefore, proposed to be eliminated.

Are there some persons currently presumed to be underwriters under Rule 145 that should continue to be presumed to be underwriters? If the presumptive underwriter standard is removed, should Rule 145 still include provisions addressing the underwriter issue with respect to resales of securities acquired in Rule 145 transactions? Would it be helpful to retain a resale safe harbor in the rule for those persons who are concerned that they might be determined to be underwriters with respect to their resales? Would it be unnecessary to retain a resale safe harbor in the rule because affiliates of the surviving company would be able to rely on Rule 144 for resales in any event?

IV. Solicitation of Comment

A. Other Possible Rule 144 Changes

The Commission solicits comment on additional revisions to Rule 144 in the two sections below. After review of the public comments on these possible revisions, the Commission may choose to adopt either or both without further solicitation of public comment.

1. Rule 144 Holding Periods

Under the Rule 144 amendments being adopted today in the Adopting Release, all restricted securities must be held at least one year before resale if Rule 144 is used, with the year measured from the date the securities were purchased from the issuer or an affiliate.[47] For restricted securities held between one and two years, other provisions of the rule require current information about the issuer to be available to the market, limit the amount of securities that may be resold, require resales to be made in ordinary brokerage transactions or directly with a market-maker,[48] and require filing with the Commission of a notification of the resale on Form 144, if the amount of securities sold exceeds specified thresholds. After a two-year holding period, restricted securities may be resold by non-affiliates without compliance with any of these provisions.[49]

There was a consensus among commenters that shortened holding periods would facilitate efforts to raise capital through private placements by shrinking the discount in price attributable to illiquidity of capital during the restricted period and allowing investors to recoup their capital faster. Two commenters, however, argued that the holding period for limited resales should be shorter than the proposed one year, with one commenter suggesting a six-month period and the other suggesting a three-month period.

The holding period requirement provides an objective criterion for determining that the securities are not being sold as part of a public distribution by the issuer. As such, this holding period should be long enough to prevent circumvention of the registration requirements by assuring that the securities are not still linked to the issuer's offering, but no longer than necessary to satisfy this purpose, so as to avoid imposing unnecessary costs or placing unnecessary restraints on the flow of capital.

The Commission seeks comment on whether the Rule 144(d) holding period after which limited resales are allowed should be shortened from one year to six months.[50] Would this period be long enough to ensure that the Rule 144 resales would not be part of an unregistered public distribution? Should the further shortening be tied to some other safeguard such as a prohibition on hedging during the holding period?

Commenters favoring a six-month holding period are asked to consider

[41] 17 CFR 230.144(i).

[42] Proposed Rule 144(f).

[43] 17 CFR 230.144(j).

[44] *See* Preliminary Note 3 to Regulation D and Preliminary Note 3 to Rule 701.

[45] Rule 145(c) [17 CFR 230.145(c)].

[46] 17 CFR 230.145(d). The companion Adopting Release amends Rule 145(d) by shortening the requisite holding periods from two and three years to one and two years, respectively, consistent with the amendments to the Rule 144 holding periods. Persons who are effecting resales of registered securities issued in Rule 145 transactions generally fall into four categories. Rule 145(d) applies to their resales as follows: (1) Non-affiliate of acquired company who is a non-affiliate of the acquiring company after the transactions—Rule 145 (c) and (d) not applicable and securities are unrestricted; (2) Non-affiliate of acquiring company who is an affiliate of the acquiring company after the transaction—Rule 145 (c) and (d) not applicable, but Rule 144 would be, if no other exemption could be found; (3) Affiliate of acquired company who is a non-affiliate of the acquiring company after the transaction—resale may be made under Rule 145(d)(1), (2) or (3); and (4) Affiliate of acquired company who is an affiliate of the acquiring company after the transaction—Rule 145(d)(1) applies.

[47] Rule 144(d) [17 CFR 230.144(d)].

[48] This requirement is proposed to be rescinded, as discussed above.

[49] Current Rule 144(k) and proposed Rule 144(g).

[50] Other provisions of the federal securities laws may offer support for a six-month holding period. For example, it may be useful to consider the six month anti-integration standard in Regulation D, which is comprised of several rules governing the limited offer and sale of securities without registration under the Securities Act. Rule 502 of Regulation D provides that offers and sales made more than six months before the start, or after the completion, of a Regulation D offering will not be considered part of that offering. Six months also is the test used in Exchange Act Section 16 to evidence a sufficient separation between purchase and sale to make recapture of ''short swing'' profits unnecessary.

whether the volume limitations [51] should be made more restrictive and/or hedging activities should be proscribed or further restricted if the holding period is reduced to six months. For example, if the Commission reduced the holding period to six months, should it also reduce by one-half, one-third, one quarter or some other measure the amount of securities that could be resold in any three-month period after completion of the holding period? Should there be a correlation between the Rule 144 volume limitations and the length of the holding period (for example, for resales between six months and one year the volume would be more limited than between one year and two years)? Should the volume limitations relate to the amount of securities to be sold in a monthly, rather than quarterly, period? If so, should the monthly volume test apply only during the six to twelve month period, or through the entire Rule 144 holding period? If a monthly test is used, should Form 144 also relate to monthly rather than quarterly sales?

Would it be appropriate to tie the volume limitations to the amount of restricted and control securities owned by the seller? For example, should the rule restrict Rule 144 sales in a quarterly period to ten percent of the amount of restricted and/or control securities owned by the seller on the date of the Rule 144 sale?

Should the holding period after which non-affiliates can sell without restriction be shorter than the two-year period adopted today, *e.g.*, one year or 18 months? Assuming the newly adopted one-year holding period is not shortened further, adoption of a one-year holding period after which non-affiliates can sell without restriction would significantly simplify the rule since it would include only one measurement period. Is a one-year holding period for unrestricted resales by non-affiliates sufficient to assure that the resales are not part of an unregistered public distribution? Should such a one-year period be adopted either alone or in conjunction with also adopting a six-month period for limited resales?

Alternatively, should the holding period for limited and unrestricted Rule 144 resales be set at a different but uniform period, such as 18 months? Would such a test strike an appropriate balance between simplifying the rule and restricting resales only in those situations that raise the risk of an indirect unregistered distribution?

[51] Rule 144(e) [17 CFR 230.144(e)].

Further comment is solicited on a number of other variations. Should the holding period depend on the size of the company? For example, would it be appropriate to implement a shorter holding period for securities of larger companies? If a shorter period were appropriate for larger companies, should it be limited to companies eligible to use Form S–3,[52] or to companies traded on national securities exchanges? Should the period be reduced for securities of larger companies to six months, while securities of all other companies would be subject to a longer holding period, such as one year? Moreover, should different holding periods be established for debt and equity securities, such as allowing unlimited resales of debt securities after six months?

2. Rule 144(e) Volume Limitations

The volume limitations in Rule 144(e) restrict the amount of restricted or control securities that can be sold.[53] Currently, the amount of these securities, together with all sales by the seller of restricted and control securities of the same class within the preceding three month period, cannot exceed the *greater* of the following three tests:

(1) one percent of the shares or other units of the class outstanding as shown by the most recent report or statement published by the issuer;

(2) the average weekly volume of trading in such securities on all national securities exchanges and/or reported through the automated quotation system of a registered securities association during the four calendar weeks preceding the filing of Form 144, or if no Form 144 is required to be filed, the date of receipt of the order to execute the transaction by the broker or the date of execution of the transaction directly with a market maker; or

(3) the average weekly volume of trading in such securities reported through the consolidated transaction reporting system during the four week period specified in (2).

The Commission solicits comment on whether the two tests based on trading volume should be eliminated. There are two reasons why the Commission is considering this possibility. First, the trading volume tests appear to needlessly complicate the rule. Based on a review of a large number of Rule 144 transaction filings by the staff, the Commission believes that most persons selling securities under Rule 144 currently rely on the shares outstanding test because it allows sufficient shares to be sold and is easier to apply than the trading volume tests. Accordingly, it could be appropriate to simplify the rule by eliminating these tests.

Second, there is an issue as to whether the trading volume limitations are comparable between different markets because of the effect on trading volume of market structure differences between the Nasdaq market and the national securities exchanges.[54] The New York Stock Exchange has submitted a rule petition asking that this be addressed.[55] According to the New York Stock Exchange petition, these differences in market structure may mean that the Rule 144 test may not provide sufficiently comparable information to form the basis for a uniform volume test.[56]

Comment is sought on the extent to which persons use the trading volume tests to calculate the number of securities they can sell in reliance on Rule 144. If the trading volume tests are kept, should one or both of the tests be adjusted to account for differences between the Nasdaq market and the national securities exchanges to determine trading volume? Should the Nasdaq volume test be one-half of the national securities exchange volume, as the New York Stock Exchange suggested, or would some smaller adjustment serve to make the tests more comparable? Do differences in trading characteristics of securities make a simple adjustment not practicable? Commenters are asked to supply supporting data, if possible.

B. Possible Regulatory Approaches to Hedging Transactions

The 1995 Release noted that recent years have evidenced the growth of a

[52] 17 CFR 239.13.

[53] The staff has taken the interpretive position that offshore resales of securities under Regulation S need not be included in the calculation of the amount of securities sold under Rule 144. The Regulation S Proposing Release proposes to codify this interpretive position.

[54] See Deborah Lohse & Dave Kansas, *Big Board is Crying Foul to Regulators Over How Nasdaq Figures Daily Volume, Wall St. J.*, August 5, 1996 at C1 and *Big Board Seeks Volume Change, N.Y.T.*, July 16, 1996 at D7.

[55] The Petition for Rulemaking was filed on July 9, 1996 and is available in File No. 4–390 in the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549.

[56] The petition asks the Commission to change Rule 144 and other rules with trading volume standards so that the standards would operate comparably in all markets. The petition asserts that dealer interpositioning on Nasdaq ''on virtually every trade approximately doubles the reported volume of trading of shares changing hands between investors, as compared with auction markets where buyers and sellers meet directly and reported volume reflects that direct interaction as a single reported trade.'' The Commission has not instituted rulemaking based on the New York Stock Exchange petition. *See* Letter to the New York Stock Exchange regarding Petition for Rulemaking, File No. 4–390 (February 19, 1997). Commenters favoring retention of a trading volume test for Rule 144 resales may wish to address the comparability issues raised by the petition.

variety of hedging strategies in both the private and public securities markets associated with separating the bundle of rights that make up a security, including voting, price appreciation and dividend rights. [57] Through the use of equity swaps [58] and similar strategies, holders of restricted securities can retain legal title to their securities, but sell some or all of the rights associated with the securities in order to decrease or eliminate the risk that the market value of their investment will decline during a specific period of time.

The 1995 Release solicited public comment on whether it is appropriate to treat the securities underlying equity swaps as ''held'' in the private markets if the economic risk of the investment has been shifted. It also stated that the Commission was examining whether it may be appropriate to revise Rule 144 to reflect the economic realities of these transactions either by reintroducing the holding period tolling concept that was deleted in 1990 for periods when the holder has entered into a hedging strategy or by prohibiting risk-shifting transactions altogether during the holding period.[59] Commenters also were asked to provide their views as to the need to have a fungibility doctrine underlie Rule 144.

Several commenters argued that hedging strategies should not be restricted or prohibited during the Rule 144 holding periods, primarily because hedging strategies do not permit holders of restricted securities to shift all of the economic risks of holding the securities to another person or the public markets and do not result in any leakage of restricted stock into the public markets. Other commenters thought that holders of restricted securities should not be engaging in hedging transactions during the holding period.

Since issuance of the 1995 Release, the Commission has given further consideration to the issue of whether the entry into equity swaps and other hedging arrangements with respect to restricted securities is inconsistent with the principles underlying the registration requirements of the Securities Act and the Rule 144 safe harbor. The Commission recognizes that arguments can be made in favor of treating ''short against the box'' transactions and equity swaps as sales of the underlying restricted securities since these transactions typically hedge fully a holder of restricted securities against any economic risk. Without risk, there is arguably no investment intent, suggesting that the holder is more of an underwriter than an investor. At the same time, it can be argued that hedging transactions do not raise Section 5 issues because the restricted securities are not being sold into the open marketplace. Instead, only freely tradeable securities are actually redistributed to the public. Proponents of this view argue that the two types of securities are not ''fungible'' or interchangeable.

The economic substance of the transactions, however, gives rise to concern. For example, it is arguable that, in economic reality, a distribution occurs when a company sells unregistered restricted stock to an investor who, in turn, hedges the market risk through an equity swap with an investment bank, which then sells an equal number of securities into the market. A staff review of industry practices found that practitioners were more concerned about the Section 5 ramifications of hedging during a short period of time following acquisition of the restricted securities (typically three months) because a disposition of risk so soon after acquisition raises questions about the nature of the investment. The industry also seems less concerned about partial hedges. Partial hedges with options may raise fewer concerns because the investment bank is less likely to sell an equal number of shares into the marketplace (thereby involving less of a distribution).

The Commission requests comment on a number of possible regulatory approaches to hedging. First, it could make the Rule 144 safe harbor unavailable for persons who hedge during the restricted period. Second, independent of Rule 144, it could promulgate a rule that would define a sale for purposes of Section 5 to include specified hedging transactions. In order to hedge, a person would need an exemption from registration for the transaction or else would have to register the transaction with the Commission. Under this approach, a hedging transaction would be treated the same as a sale of the underlying security, so hedging would be constrained in the same way (*e.g.*, if an exemption is used such as Rule 144, the Rule 144 volume restrictions would apply). Third, as a variant of the first approach, it could adopt a shorter holding period (*e.g.*, three or six months) during which hedging could not occur without losing the safe harbor. After that, hedging could occur, but the underlying restricted securities would be held the remainder of the one-year holding period adopted today. Fourth, it could reintroduce a tolling provision in Rule 144 similar to the provision that was included prior to 1990. The last approach would be to maintain the status quo with no specific prohibition against hedging, relying instead upon practitioners to apply a facts and circumstances test to determine when Section 5 is implicated. Comment is solicited generally on each of the above approaches.

For purposes of a definition, the Commission is considering defining hedging to include any sale or combination of swap, option, or short sale intended to limit or eliminate the market risk of restricted or control stock. Alternatively, the Commission could use the definition of ''put equivalent'' position in Exchange Act Rule 16a–1(h).[60] Should the definition be expanded to include futures, contracts, ''collars'' or other instruments that operate similarly to a swap or option?

If the second overall approach were adopted, should all hedging be considered a sale for purposes of Section 5? If not, should only transactions like swaps and short sales of securities of the same class as the restricted securities be deemed sales because they most closely approximate a sale of the restricted securities? If options are included, should there be a

[57] Hedging is a risk limiting device much like buying insurance. For example, a person could hedge common stock by purchasing a put option to sell the common stock at a fixed price. If the stock value increases, the holder profits. If the stock price falls, the put option can be exercised to sell the stock at a predetermined price.

[58] Equity swaps are individually negotiated contracts, the specific terms of which may vary from agreement to agreement. One form of equity swap involves an agreement by a holder of equity securities to pay, or ''swap,'' the return on the securities (which may include dividends as well as any change in market value) in exchange for the return on an equity index, basket of securities, or an interest-rate based cash flow.

[59] Deletion of the tolling provision in 1990 did not mean that holders could freely engage in hedging activities with respect to their restricted securities without consideration of the registration requirements. The Commission staff historically has viewed the question of whether a hedging transaction would toll the holding period as separate from the question of whether a hedging transaction was subject to Section 5 of the Securities Act. With respect to short sales ''against the box,'' (meaning that the person sells short even though the person owns securities that can be delivered) the Division continues to take the position expressed in the 1979 Rule 144 interpretative release (Release No. 33–6099, (August 2, 1979) [44 FR 46572]) that a person who has held restricted securities for less than one year cannot effect a short sale of securities of that class and then cover the short position with restricted securities (even after expiration of the one year holding period) since the initial short sale did not qualify under Rule 144. Similarly, exchange-traded puts and calls may be used for Rule 144 sales, but in the case of restricted securities, the one-year holding period requirement of Rule 144(d) must have been satisfied by the date the put is purchased or call is sold. *See Bear Stearns & Co., Inc.*, (April 4, 1991) and Release 33–6099.

[60] 17 CFR 240.16a–1(h).

difference between in-the-money options (which are likely to be exercised) and out-of-the-money options (which are less likely to be exercised)? For example, should transactions involving options be ignored if the options are sufficiently out-of-the-money (*e.g.*, 5%, 10%, 20%)? Should there be different treatment for hedging with cash settled derivative securities since their exercise does not result in any distribution of securities into the market? Should hedging a transaction be considered a sale of the underlying security only if it results in a sale of securities of the same class as the underlying security to a third party?

Since hedging can be a dynamic process, should there be a difference between the initial hedge and a subsequent ''maintenance'' hedge? For example, a holder of restricted securities might hedge only a portion of the market risk initially. As the value of the securities fluctuates, the holder may have to adjust the hedge by buying more put options, for example, or selling more stock short to maintain the same risk as initially envisioned. Presumably, this adjustment has less distributive aspects than the initial hedge. Should it make a difference if the security being hedged is control stock rather than restricted stock?

Should control stock be treated differently in general? It is not uncommon for individual affiliates to have a significant portion of their net worth represented by control or restricted stock. Such persons might want to diversify or limit their risk through hedging. Should the Commission adopt a rule that permits some limited hedging by these persons without raising Section 5 concerns? If such a safe harbor were crafted, should it be limited to a percentage of the affiliate's total holdings of control stock (*e.g.*, 5%, 10%, 20% or even 49%)? Is it sufficient to permit only hedging in accordance with the volume limitations of Rule 144(d)?

C. General Request for Comment

Any interested persons wishing to submit comment on any of the proposals set forth in this release are invited to do so by submitting them in triplicate to Jonathan G. Katz, U.S. Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. Comments also may be submitted electronically at the following e-mail address: rule-comments @sec.gov. All comment letters should refer to File Number S7–07–97; this file number should be included on the subject line if e-mail is used. Comments received will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549. Electronically submitted comment letters will be posted on the Commission's Internet Web site (http://www.sec.gov). Comments are solicited from the point of view of issuers, holders of restricted and control securities, investment bankers and the investing public.

V. Cost-Benefit Analysis

The proposed amendments, if adopted, should reduce the costs of complying with the Rule 144 safe harbor requirements by making the rule easier to understand and apply. Elimination of the manner of sale requirements would result in fewer brokerage commissions being paid by persons reselling securities in reliance on the Rule 144 safe harbor, since resale transactions no longer would have to involve a broker or market-maker. The proposed increase in Form 144 filing thresholds would result in fewer filings and also reduce compliance costs.

For purposes of the Small Business Regulatory Enforcement Act of 1996, the Commission also is requesting information regarding the potential impact of the proposed rules on the economy on an annual basis. Commenters should provide empirical data to support their views.

The Commission does not believe that the proposed amendments would have an adverse effect on competition, employment, investment, productivity, innovation, market efficiency, or capital formation. In fact, the Commission believes that the proposed amendments will promote capital formation and efficient, competitive markets by enhancing investors' confidence in the integrity of the securities markets. However, the Commission requests comment on these preliminary views. The Commission encourages commenters to provide empirical data or other facts to support their views.

VI. Initial Regulatory Flexibility Analysis

This Initial Regulatory Flexibility Analysis has been prepared in accordance with Section 603 of the Regulatory Flexibility Act,[61] and relates to the proposed amendments to Rules 144 and 145 and Form 144 under the Securities Act.

Reasons for, and Objectives of, Proposed Action

Rule 144 provides a safe harbor for the resale of restricted and control securities. It sets forth conditions which, if satisfied, permit persons who hold such securities to publicly sell them without registration and without being deemed underwriters.

Rule 145 governs the offer or sale of securities received in connection with reclassifications, mergers, consolidations and asset transfers. It provides that any party to a transaction covered by the rule (other than the issuer), or any person who is an affiliate of such party at the time the transaction is submitted for vote or consent, who publicly offers or sells securities of the issuer acquired in connection with such a transaction will be deemed to be engaged in a distribution, and therefore to be an underwriter of the securities, except where the securities are resold in accordance with Rule 145(d). Rule 145(d) requires its own holding periods that track the holding periods for resales found in Rule 144.

Form 144 is required to be filed by persons intending to sell securities in reliance on Rule 144 if the amount of securities to be sold in any three month period exceeds 500 shares or other units or the aggregate sales price exceeds $10,000. The primary purpose of the form is to publicly disclose the proposed sale of unregistered securities by persons not deemed to be engaged in the distribution of securities.

The Commission has determined to propose amendments that would make Rule 144 easier to understand and apply. The staff has reorganized and shortened the rule to make it easier to understand and apply. In addition to codifying certain staff interpretive positions, the proposals would make the following substantive changes to Rule 144:

- Provide a bright-line exclusion from the Rule 144 definition of affiliate. Pursuant to the proposal, persons who would not be subject to the provisions of Section 16, *i.e.*, persons who are not officers, directors or 10% holders of the issuer, would be deemed not to be affiliates of an issuer for purposes of Rule 144;
- Eliminate the manner of sale requirements; and
- Increase the thresholds for filing Form 144 from the current 500 shares or $10,000 sale price test to a 1000 shares or $40,000 sale price test.

The proposals also would amend Rule 145, which relates to certain significant transactions, such as mergers, to eliminate the resale limitations that are based on a ''presumptive underwriter'' approach. Instead of that approach, persons who receive securities in these transactions would be treated the same as other purchasers of securities.

[61] 5 U.S.C. § 603.

The revision to the definition of affiliate would provide more objective guidance for issuers and sellers of securities as to the types of persons that are not affiliates for purposes of Rule 144. Elimination of the manner of sale requirements would remove obstacles to transactions that are not distributive in nature. An increase in the Form 144 filing thresholds would take into account the effects of inflation since adoption of Rule 144 in 1972.

The release solicits comment on shorter Rule 144(d) and/or 144(k) holding periods. Persons holding restricted and control stock, including small entities holding such stock, and all issuers, including small business issuers, would benefit from shortened holding periods. The release also solicits comment on elimination of the trading volume limitation in Rule 144(e). It is unlikely that this change would have a significant economic impact on persons holding restricted and control stock, including small entities owning such stock.

Legal Basis

The amendments are proposed pursuant to Sections 2(11), 4(1), 4(4) and 19(a) of the Securities Act.

Small Entities Subject to Requirements

The proposed rules will affect both small entities that issue restricted or control securities and small entities that hold such securities. When used with reference to an issuer, other than an investment company, the term ''small business'' is defined by Securities Act Rule 157 as an issuer whose total assets on the last day of its most recent fiscal year were $5 million or less and is engaged or proposing to engage in small business financing. An issuer is considered to be engaged in small business financing if it is conducting or proposes to conduct an offering of securities that does not exceed the dollar limitation prescribed by Section 3(b) of the Securities Act. When used with reference to an issuer or person, other than an investment company, Exchange Act Rule 0–10[62] defines small entity to mean an issuer or person that, on the last day of its most recent fiscal year, had total assets of $5,000,000 or less.[63]

The Commission is aware of approximately 1,019 Exchange Act reporting companies that currently satisfy the definition of ''small business'' under Rule 157 and may be affected by the proposed rules. The proposed rules also may affect small businesses that are not subject to Exchange Act reporting requirements. The Commission is unable to determine the number of such small businesses due to the absence of filings with the Commission by such companies. Comment is solicited on the number of small businesses that are not subject to Exchange Act reporting requirements that may be affected by the proposed rules.

An estimated 3,800 entities, excluding natural persons, annually file Form 144 based upon a sample study of Form 144 filings by the Commission's Office of Economic Analysis. Since the form does not require disclosure of the size of entities reselling securities in reliance on Rule 144, the Commission has no basis for estimating the number of these entities that are small entities. Comment is solicited as to the number of small entities who may rely on Rule 144 in reselling restricted or control securities if the proposed rules are adopted.

The proposals would favorably affect small businesses and small entities owning restricted or control securities of issuers by improving the usefulness of the Rule 144 safe harbor and removing unnecessary and outdated requirements.

Reporting, Recordkeeping and Other Compliance Requirements

If the change to the definition of affiliate is adopted, it is expected that fewer persons, including small entities, owning restricted and control stock of all issuers, including small issuers, will file Form 144. The reduction would result from the fact that some persons who are not officers, directors or 10% holders of an issuer presumably consider themselves to be affiliates under the current Rule 144 definition. The Commission has no basis, however, for estimating the size of this expected decrease since it does not collect any information that would provide a basis for such an estimate and such information is not otherwise available to the Commission. Comment is solicited as to how to quantify the expected decrease.

If the manner of sale requirements were eliminated, persons (including small entities) owning restricted and control stock of all issuers, including small issuers, no longer would have to sell their stock in a broker's transaction or directly with a market-maker. Those choosing to sell their stock in a transaction not involving a broker or market-maker would not incur the expense of commission fees.

Adoption of increased share number and dollar amount thresholds for filing Form 144 also is expected to decrease the number of Form 144 filings required to be made by persons (including small entities) owning restricted and control stock of all issuers, including small issuers. Based on studies by the Commission's Office of Economic Analysis, the number of Form 144 filings is expected to decrease by approximately 5% (1,339 filings) if the thresholds are increased to 1,000 shares or $40,000 in market value.

The release solicits comment on whether the thresholds should be increased as high as 2,000 shares or $100,000. It is estimated that if these higher thresholds were adopted, the number of Form 144 filings would decrease by approximately 14% (3,677 filings).

Finally, some persons (including small entities) owning stock in issuers, including small issuers, that engage in the type of transactions covered by Rule 145 would benefit from the proposed revisions since there no longer would be a presumption that persons who receive securities in these transactions are underwriters. The Commission has no basis for estimating the number of persons who may be deemed to be underwriters under the current rule that would not be determined to be underwriters if the proposed change is adopted since it does not collect any information that would provide a basis for such an estimate and such information is not otherwise available to the Commission. Comment is solicited as to how to quantify such number.

Clerical skills are necessary to complete Form 144.

Overlapping or Conflicting Federal Rules

No current federal rules duplicate, overlap or conflict with the rules and forms to be proposed, except that persons subject to the reporting requirements under Section 16 of the Securities Exchange Act of 1934 may need to file reports on Form 4 as well as Form 144 under certain circumstances.

Significant Alternatives

The Commission considered the establishment of different compliance standards for small entities owning restricted and control securities, as well as for persons owning restricted and control securities of small issuers. For example, the Commission could establish shorter holding periods or more lenient Form 144 filing requirements. Such differences, however, would be inconsistent with the purposes served by the holding period and Form 144 filing requirements and would needlessly

[62] 17 CFR 240.0–10.

[63] There is no comparable definition of ''person'' under the Securities Act.

complicate the Form 144 filing requirements. The Commission also considered the other types of alternatives set forth in section 603 of the Regulatory Flexibility Act to minimize the economic impact of the amendments on small entities: (1) the clarification, consolidation, or simplification of compliance and reporting requirements for such small entities; (2) the use of performance rather than design standards; and (3) an exemption from coverage of the proposed amendments, or any part thereof, for small entities. Because the proposed amendments would benefit all issuers and holders of restricted securities, differing compliance timetables for small entities would not be appropriate. Neither could the compliance requirements of the amendments be clarified or simplified further for small entities. Finally, the proposed amendments do not use design standards, and an exemption from the amendments for small entities would not be desirable or consistent with the stated objectives of the applicable statutes.

Solicitation of Comments

Written comments are encouraged with respect to any aspect of this Initial Regulatory Flexibility Analysis. In particular, the Commission seeks comment on: (i) the number of small entities that would be affected by the proposed rule; (ii) the expected impact of the proposals as discussed above; and (iii) how to quantify the number of small entities that would be affected by, and how to quantify the impact of, the proposed rules. Commenters are asked to describe the nature of any impact and provide empirical data supporting the extent of the impact. Such comments will be considered in the preparation of the Final Regulatory Flexibility Analysis if the proposed revisions are adopted. Persons wishing to submit written comments should file them with Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. All comments received will be available for public inspection and copying at the Commission's Public Reference Room at the same address.

VII. Paperwork Reduction Act

Form 144 contains ''collection of information'' requirements within the meaning of the Paperwork Reduction Act of 1995 (''PRA'').[64] The Commission has submitted the proposed revisions to Form 144 to the Office of Management and Budget for review in accordance with PRA procedures.[65] The title for the information collection is ''Notice of Proposed Sale of Securities Pursuant to Rule 144 under the Securities Act of 1933.''

As proposed to be revised, Form 144 would be filed with the Commission by persons who intend to sell securities in reliance on Rule 144 if the amount of securities to be sold during a three-month period exceeds 1,000 shares or other units or has an aggregate sales price in excess of $40,000. The proposed thresholds for filing Form 144 would be increased from existing thresholds of 500 shares or a $10,000 sale price. Form 144 may be filed electronically using the EDGAR filing system. The information is used for the primary purpose of disclosing the proposed sale of unregistered securities by persons deemed not to be engaged in the distribution of the securities. It is made publicly available. Persons reselling securities in reliance on the Rule 144 safe harbor are the likely respondents to the information required by Form 144.

An estimated 18,096 respondents are expected to file Form 144 annually for a total burden of 36,192 hours if the proposed revisions to Form 144 are adopted. This represents a decrease of 2,678 hours from the current annual burden under existing thresholds. The information collection requirements imposed by Form 144 are mandatory. The Commission may not require Form 144 filings unless the form displays a currently valid OMB control number.

The Commission solicits comment to: (i) evaluate whether Form 144, as proposed to be revised, is necessary for the proper performance of the functions of the agency, including whether the information shall have practical utility; (ii) evaluate the accuracy of the agency's estimate of the burden of the proposed collection of information; (iii) enhance the quality, utility, and clarity of the information to be collected; and (iv) minimize the burden of collection of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

Persons desiring to submit comments on the collection of information requirements should direct them to the Office of Management and Budget, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, D.C. 20503, and should also send a copy of their comments to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 5th Street, N.W., Washington, D.C. 20549 with reference to File No. S7–07–97. OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication, so a comment to OMB is best assured of having its full affect if OMB receives it within 30 days of publication.

VIII. Statutory Basis

The amendments to Rules 144 and 145 and Form 144 are being proposed pursuant to sections 2(11), 4(1), 4(4) and 19(a) of the Securities Act.

List of Subjects in 17 CFR Parts 230 and 239

Reporting and recordkeeping, Securities.

Text of the Proposals

For the reasons set out above, title 17, chapter II of the Code of Federal Regulations is proposed to be amended as follows:

PART 230—GENERAL RULES AND REGULATIONS, SECURITIES ACT OF 1933

1. The authority citation for Part 230 continues to read in part, as follows:

Authority: 15 U.S.C. 77b, 77f, 77g, 77h, 77j, 77s, 77sss, 78c, 78d, 78*l*, 78m, 78n, 78o, 78w, 78*ll*(d), 79t, 80a–8, 80a–29, 80a–30, and 80a–37, unless otherwise noted.

* * * * *

2. Section 230.144 is amended by revising the Preliminary Note, paragraphs (a)(1), (a)(3), (b), and (c), adding notes to paragraph (c), revising paragraphs (d)(3)(ii), (d)(3)(vi), (d)(3)(vii) and (d)(3)(viii), adding paragraph (d)(3)(ix), revising the introductory text of paragraph (e)(1), revising paragraph (e)(2), removing paragraphs (f) and (g), re-designating paragraph (h) as paragraph (f), removing paragraphs (i) and (j), re-designating paragraph (k) as paragraph (g) and by revising newly designated paragraphs (f) and (g) to read as follows:

§ 230.144 Persons deemed not to be engaged in a distribution and therefore not underwriters.

Preliminary Note

The Securities Act of 1933 requires that all offers and sales of securities in interstate commerce or by use of the mails must be registered with the Commission or exempt from registration. While Section 4(1) exempts most routine trading, transactions by underwriters are not exempt. Rule 144 creates safe harbor exemptions for two common situations arising from the Act's definition of ''underwriter.''

First, anyone who has taken securities directly from the issuer in an unregistered

[64] 44 U.S.C. § 3501 *et seq.*

[65] 44 U.S.C. § 3507(d) and 5 CFR § 1320.11.

transaction and who effects a public resale in the short term may be said to be a ''person who has purchased from an issuer with a view to * * * distribution,'' and thus an ''underwriter'' within the meaning of Section 2(11) of the Act. An investment banking firm that arranges with an issuer for the public sale of its securities is clearly an ''underwriter'' under that Section. Individual investors who are not professionals in the securities business may also be ''underwriters'' within the meaning of that term as used in the Act if they act as links in a chain of transactions through which securities move from an issuer to the public. Rule 144 provides an exemptive safe harbor for the resale of these ''restricted securities.''

Second, Section 2(11) treats persons in a relationship of control with the issuer (''affiliates'') as if they were the issuer for the purpose of determining which intermediaries to the public markets are ''underwriters.'' As a result, a public sale of an affiliate's securities (''control securities''), whether or not the securities are ''restricted,'' is subject to the same regulatory requirements as a public offering by the issuer. Rule 144 provides an exemptive safe harbor for the resale of control securities on behalf of an affiliate of the issuer.

Rule 144 sets forth certain conditions which are intended to distinguish between a distribution and routine trading. First, adequate current public information is required to protect investors. Second, a holding period before resale is needed to assure that persons who buy restricted securities in unregistered offerings have assumed the economic risks of investment and are not acting as conduits for the issuer in an unregistered public distribution. Third, Rule 144 requires a person relying on the Rule to sell the securities in limited quantities to further demonstrate that trading is ordinary, rather than distributive.

If a sale of securities is made in accordance with all of the provisions of Rule 144, (1) any person who sells restricted securities will be deemed not to be an underwriter for that transaction; (2) any person who sells restricted or other securities on behalf of an affiliate of the issuer will be deemed not to be an underwriter for that transaction; and (3) the purchaser receives unrestricted securities.

Rule 144 is not an exclusive safe harbor. It does not affect the availability of any other exemption for resales under the Securities Act.

(a) * * *

(1) An *affiliate* of an issuer is a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, such issuer. A person shall be deemed not to be an affiliate for purposes of this section if the person:

(i) Is not the beneficial owner, directly or indirectly, of more than 10% of any class of equity securities of the issuer;

(ii) Is not an officer of the issuer; and

(iii) Is not a director of the issuer.

Note to paragraph (a)(1): The determination of a person's beneficial ownership and whether that person is an ''officer'' shall be made in accordance with § 240.16a–1 of this chapter, regardless of whether the issuer's securities are subject to Section 16 (15 U.S.C 78(p)) of the Securities Exchange Act of 1934 (''Exchange Act'') and regardless of whether the class of securities is registered under Section 12 (15 U.S.C. 78*l*) of the Exchange Act.

* * * * *

(3) The term *restricted securities* means:

(i) Securities acquired directly or indirectly from the issuer, or from an affiliate of the issuer, in a transaction or chain of transactions not involving any public offering;

(ii) Securities acquired from the issuer that are subject to the resale limitations of § 230.502(d) under Regulation D or § 230.701(c);

(iii) Securities acquired in a transaction or chain of transactions meeting the requirements of § 230.144A;

(iv) Securities acquired from the issuer in a transaction subject to the conditions of Regulation CE (§ 230.1001);

(v) Equity securities of domestic issuers, and of foreign issuers where the principal market for such securities is in the United States, acquired in a transaction or chain of transactions subject to the conditions of § 230.901 or § 230.903 under Regulation S (§§ 230.901 thru 230.905 and Preliminary Notes); or

(vi) Securities acquired from the issuer that were issued pursuant to an exemption under section 4(6) (15 U.S.C. 77(d)(6)) of the Act.

(b) *Conditions to be met.* (1) Any affiliate or other person who sells restricted securities of an issuer for such person's own account shall be deemed not to be an underwriter thereof within the meaning of section 2(11) (15 U.S.C. 77(b)(11)) of the Act if all of the conditions of this section are met.

(2) Any person who sells restricted or any other securities for the account of an affiliate of the issuer of such securities shall be deemed not to be an underwriter thereof within the meaning of Section 2(11) of the Act if all of the conditions of this section are met.

(c) *Current public information.* Adequate current public information with respect to the issuer of the securities must be available. Such information will be deemed to be available only if either of the following conditions is met:

(1) *Reporting Issuers.* The issuer is, and for at least 90 days before the sale has been, subject to the reporting requirements of Section 13 or 15(d) of the Exchange Act (15 U.S.C. 78(m) or (o)(d)) and has filed all required reports during the 12 months preceding such sale (or for such shorter period that the issuer was required to file such reports); or

(2) *Non-reporting Issuers.* If the issuer is not subject to the reporting requirements of Section 13 or 15(d) of the Exchange Act, there is publicly available the information concerning the issuer specified in paragraph (a)(5)(i) to (xiv), inclusive, and paragraph (a)(5)(xvi) of § 240.15c2–11 of this chapter, or, if the issuer is an insurance company, the information specified in Section 12(g)(2)(G)(i) of the Exchange Act.

Notes to paragraph (c): 1. With respect to paragraph (c)(1), the seller can rely upon:

(A) A statement in whichever is the most recent report, quarterly or annual, required to be filed and filed by the issuer that such issuer has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the issuer was required to file such reports) and has been subject to such filing requirements for the past 90 days; or

(B) A written statement from the issuer that it has complied with such reporting requirements. Neither type of statement may be relied upon, however, if the person knows or has reason to believe that the issuer has not complied with such requirements.

2. Rule 144(c) cannot be satisfied during the first 90 days after an issuer becomes subject to the reporting requirements of Section 13 or 15(d) of the Securities Exchange Act.

(d) * * *

(3) * * *

(ii) *Conversions and exchanges.* If the securities sold were acquired from the issuer solely in exchange for other securities of the same issuer, the newly acquired securities shall be deemed to have been acquired at the same time as the securities surrendered for conversion or exchange, even if the securities surrendered were not convertible or exchangeable by their terms;

* * * * *

(vi) *Trusts.* Where a trust settlor is an affiliate of the issuer, securities acquired from the settlor by the trust, or acquired from the trust by the beneficiaries, shall be deemed to have been acquired when they were acquired by the settlor.

(vii) *Estates.* Where a deceased person was an affiliate of the issuer, securities held by the estate of such person or acquired from such an estate by the beneficiaries shall be deemed to have been acquired when they were acquired by the deceased person. Regardless of whether the deceased person was an affiliate of the issuer, no further holding period is required if the estate is not an affiliate of the issuer or if the securities

are sold by a beneficiary of the estate who is not an affiliate.

(viii) *Rule 145(a) transactions.* The holding period for securities acquired in a transaction specified in § 230.145(a) shall be deemed to commence on the date the securities were acquired by the purchaser in such transaction, except as otherwise provided in paragraphs (d)(3)(ii) and (ix) of this section.

(ix) *Holding company formations.* Securities acquired from the issuer in a transaction effected solely for the purpose of forming a holding company shall be deemed to have been acquired at the same time as the securities of the predecessor issuer exchanged in the holding company formation where:

(A) The holding company's securities were issued in a transaction involving an exchange of securities as part of a reorganization of the predecessor into a holding company structure;

(B) Holders received securities of the same class evidencing the same proportional interest in the holding company as they held in the predecessor; and

(C) Immediately following the transaction, the holding company has no significant assets other than securities of the predecessor and its existing subsidiaries and has substantially the same assets and liabilities on a consolidated basis as the predecessor had prior to the transaction.

(e) * * *

(1) *Sales by affiliates.* If any securities are sold for the account of an affiliate of the issuer, regardless of whether those securities are restricted, the amount of securities sold, together with all sales of securities of the same class sold for the account of such person within the preceding three months, shall not exceed the greatest of:

* * * * *

(2) *Sales by persons other than affiliates.* The amount of restricted securities sold for the account of any person other than an affiliate of the issuer, together with all other sales of restricted securities of the same class sold for the account of such person within the preceding three months, shall not exceed the greatest of the amounts specified in paragraphs (e)(1)(i), (ii) or (iii) of this section, whichever is applicable.

* * * * *

(f) *Notice of proposed sale.* (1) If the amount of securities to be sold in reliance upon this section during any period of three months exceeds 1,000 shares or other units or has an aggregate sale price in excess of $40,000, three copies of a notice on Form 144 (§ 239.144 of this chapter) shall be filed with the Commission at its principal office in Washington, DC. If such securities are admitted to trading on any national securities exchange, one copy of such notice also shall be transmitted to the principal exchange on which such securities are admitted.

(2) The Form 144 shall be signed by the person for whose account the securities are to be sold and shall be transmitted for filing concurrently with either the sale of securities in reliance upon this section or the placing with a broker of an order to sell securities in reliance upon this section. Neither the filing of such notice nor the failure of the Commission to comment thereon shall be deemed to preclude the Commission from taking any action it deems necessary or appropriate with respect to the sale of the securities referred to in such notice. The person filing the notice required by this paragraph shall have a bona fide intention to sell the securities referred to therein within a reasonable time after the filing of such notice.

(g) *Termination of certain restrictions on sales of restricted securities by persons other than affiliates.* The requirements of paragraphs (c), (e) and (f) of this section shall not apply to the sale of restricted securities if:

(1) The sale is for the account of a person who is not an affiliate of the issuer at the time of the sale and who has not been an affiliate of the issuer during the three months preceding the sale; and

(2) A period of at least two years has elapsed since the later of the date the securities were acquired from the issuer or from an affiliate of the issuer. The two-year period should be calculated as described in paragraph (d) of this section.

3. By amending § 230.145 by removing paragraphs (c) and (d) and re-designating paragraph (e) as paragraph (c).

* * * * *

PART 239—FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933

4. The authority citation for part 239 continues to read in part as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77sss, 78c, 78l, 78m, 78n, 78o(d), 78w(a), 78ll(d), 79e, 79f, 79g, 79j, 79l, 79m, 79n, 79q, 79t, 80a–8, 80a–29, 80a–30 and 80a–37, unless otherwise noted.

* * * * *

5. By amending § 239.144 by revising paragraphs (a) and (b) to read as follows:

§ 239.144. Form 144, for notice of proposed sale of securities pursuant to § 239.144 of this chapter.

(a) Except as indicated in paragraph (b) of this section, this form shall be filed in triplicate with the Commission at its principal office in Washington, DC by each person who intends to sell securities in reliance upon § 230.144 of this chapter and shall be transmitted for filing concurrently with either the execution of a sale of securities in reliance upon § 230.144 of this chapter or the placing with a broker of an order to execute a sale of securities in reliance upon § 230.144 of this chapter.

(b) This form need not be filed if the amount of securities to be sold during any period of three months does not exceed 1,000 shares or other units and the aggregate sale price does not exceed $40,000.

* * * * *

6. By amending Form 144 (referenced in § 239.144) by revising the statement appearing under the Form title, revising the caption to Item 3(b) in the undesignated table, removing the ''s'' at the end of ''Instructions'' after Table I, removing Instruction 2 to Table I, and removing the designation number for the remaining instruction to read as follows:

Note: The text of Form 144 does not, and the amendments thereto will not, appear in the Code of Federal Regulations.

Form 144

Notice of Proposed Sale of Securities Pursuant to Rule 144 Under the Securities Act of 1933

Attention: Transmit for filing 3 copies of this form concurrently with either placing an order with a broker to execute a sale or executing a sale directly with a market maker, or at the time of executing a sale not involving a broker or market maker.

* * * * *

Item 3(b). Name and Address of Each Broker Through Whom the Securities are to be Offered or Each Market Maker who is Acquiring the Securities, if Applicable

* * * * *

Table I—Securities To Be Sold

* * * * *

Instruction if the securities were purchased and full payment therefore was not made in cash at the time of purchase, explain in the table, or in a note thereto, the nature of the consideration given. If the consideration consisted of any note or other obligation, or if payment was made in installments, describe the arrangement and state when the note or other

obligation was discharged in full or the last installment paid.

By the Commission.

Dated: February 20, 1997.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 97–4667 Filed 2–27–97; 8:45 am]

BILLING CODE 8010–01–P

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 228, 229, 230, and 249

[Release No. 33–7392; 34–38315; File No. S7–8–97 International Series Release No. 1056]

RIN 3235–AG34

Offshore Offers and Sales

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rules.

SUMMARY: The Securities and Exchange Commission (the ''Commission'') is publishing for comment proposed amendments to the Regulation S safe harbor procedures. The proposed amendments 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 proposals are designed to stop abusive practices in connection with offerings of equity securities purportedly made in reliance on Regulation S.

DATES: Comments should be received on or before April 29, 1997.

ADDRESSES: Comments should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Stop 6–9, Washington, D.C. 20549. Comment letters also may be submitted electronically to the following electronic mail address: rule-comments@sec.gov. Comment letters should refer to File No. S7–8–97; this file number should be included in the subject line if electronic mail is used. All comment letters received will be available for public inspection and copying in the Commission's public reference room, 450 Fifth Street, N.W., Washington, D.C. 20549. Electronically submitted comment letters will be posted on the Commission's Internet Web site (http://www.sec.gov).

FOR FURTHER INFORMATION CONTACT: Paul M. Dudek, Luise M. Welby, or Walter G. Van Dorn, Jr., Office of International Corporate Finance, Division of Corporation Finance, at (202) 942–2990.

SUPPLEMENTARY INFORMATION: The Commission is proposing to revise Rule 903 [1] of Regulation S,[2] the issuer safe harbor under the Securities Act of 1933 [3] for offshore offerings of securities, to address abusive practices under the rule. The changes would apply to offshore sales of equity securities of domestic issuers, and of foreign issuers where the principal market for those securities is in the United States.[4] Further, the Commission proposes amendments to Rule 144(a)(3) [5] and a new Rule 905 to deem these equity securities to be ''restricted securities,'' as defined in Rule 144 under the Securities Act.[6] New Rule 905 also would make clear that offshore resales under Rule 904 of restricted equity securities of covered issuers will not affect the status of these securities as restricted securities after the resale.[7] In addition, the Commission is proposing to eliminate the current requirement that reporting issuers disclose Regulation S sales of equity securities on a Form 8–K within 15 days of the transaction. In light of the longer restricted period proposed today, issuers would report these sales on a Form 10–Q on the same basis that issuers report their other unregistered sales of equity securities. Finally, the Commission is proposing additional technical and clarifying revisions to Regulation S, in part to make the rule more concise and understandable.

I. Executive Summary

The Commission constantly seeks to reduce burdens on capital formation as long as the deregulatory measures do not harm investor protection. When adopting safe harbors and other deregulatory measures, the Commission will include protections designed to minimize the risk that those measures will be abused. If abuses nevertheless occur, the Commission will make the necessary adjustments to prevent further abuse while, to the extent possible, preserving the original goals of the reform. Today, the Commission is proposing amendments to Regulation S to prevent continued abuse of the rule.

In 1990, the Commission adopted Regulation S to clarify the extraterritorial application of the registration requirements of the Securities Act. In the interests of both comity and the internationalization of the world's securities markets, the Commission believed that the registration provisions under U.S. law should not apply where the offshore placements were truly offshore. Instead, the laws of the foreign jurisdiction regulating the public offerings of securities would serve to protect investors in that market. Regulation S permits both foreign and domestic issuers to avail themselves of the safe harbors when conducting offshore placements of their securities.

Since the adoption of Regulation S in 1990, the Commission has become aware of uses of Regulation S that the rule not only did not contemplate, but in fact expressly prohibited. Some issuers, affiliates and others involved in the distribution process are using Regulation S as a guise for distributing securities into the U.S. markets without the protections of registration under Section 5 of the Securities Act. In June 1995, the Commission issued an interpretive release that listed certain problematic practices under Regulation S and requested comment on whether the Regulation should be amended to limit its vulnerability to abuse.[8]

As a result of the continuation of certain of these abusive practices and in response to the comment letters received on the Interpretive Release, the Commission is proposing to stop these abusive practices by amending Regulation S for placements of equity securities by domestic companies. In addition, although abusive practices involving the equity securities of foreign issuers are not as evident as with domestic issuers, there is equal potential for abuse where the principal trading market for those securities is in the United States. Therefore, the Commission also is proposing to amend the safe harbor procedures for placements of equity securities of foreign issuers where the principal market for those securities is in the United States. In general, the ''principal market'' would be in the United States if more than half of the trading in that security takes place in the United States.[9]

These Regulation S proposals would:

- classify these equity securities placed offshore under Regulation S as ''restricted securities'' within the meaning of Rule 144;
- align the Regulation S restricted period for these equity securities with the Rule 144 holding periods by lengthening from 40 days

[1] 17 CFR 230.903.

[2] 17 CFR 230.901–230.904 and Preliminary Notes.

[3] 15 U.S.C. 77a *et seq.* (the ''Securities Act'').

[4] *See* Proposed Rule 902(h) for the proposed definition of ''principal market in the United States.''

[5] 17 CFR 230.144(a)(3).

[6] Proposed Rule 905.

[7] *Id.*

[8] Securities Act Release No. 7190 (June 27, 1995) [60 FR 35663 (July 10, 1995)] (the ''Interpretive Release'').

[9] *See infra* Section III.E.1. for a further discussion of the proposed definition of ''principal market in the United States.''