

Book Review

D. GOLDWASSER, *A GUIDE TO RULE 144* (2d ed. 1978) (\$40.00, Practising Law Institute, 810 Seventh Avenue, New York, New York 10019).

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Rule 144 has been described as an attempt by the SEC to change "from theology to arithmetic" the factors determining when and how letter stock and control stock may be sold without registration under the Securities Act of 1933.¹ Dan L. Goldwasser's new edition of *A GUIDE TO RULE 144* is an immensely useful compilation of the results of this shift, and is a critical guide to those parts of the catechism which have departed from the statutory philosophy.

The evolution of Rule 144 is carefully traced. Examination of early versions of what was to become Rule 144 sheds helpful light on the interpretation of the final product. Such legislative history has a way of becoming lost to those who did not live through its development. Thus, the preservation of this history in a readily accessible form would alone justify the publication of this volume. The book, however, does much more. It compiles for the lawyer, familiar with Rule 144, the gloss placed upon it by some 1500 interpretive letters from SEC's staff. This is its real contribution.

Many of the staff interpretations would, no doubt, surprise the attorney who studied carefully only the statute, Rule 144 itself, and formal releases interpreting the rule. Mr. Goldwasser explores crevices and loopholes in the rule which have been suggested by hundreds of staff interpretations. His analysis, however, inevitably raises a more basic question. This is the question of the propriety of developing such an elaborate body of law through nonadversary interpretive rulings, largely unreviewed and unreviewable.²

Prior to 1970, no-action and interpretive letters of the Commission's staff were generally unavailable.³ Professor Kenneth Culp Davis argued that "some of the most important law of the SEC is embodied in this bid batch of no action letters. This is law. The interpretations are law. . . . [S]ecret law is an abomination."⁴ The then presiding chairman, Manny Cohen, replied: "This is not secret law. It is true that

1. The description is that of SEC Chairman, William Casey's, quoted in D. GOLDWASSER, *A GUIDE TO RULE 144*, at 61 (2d ed. 1978) (Practising Law Institute) [hereinafter cited as GOLDWASSER].

2. See Lowenfels, *SEC No-Action Letters: Conflicts With Existing Statutes, Cases, and Commission Releases*, 59 VA. L. REV. 303, 319-22 (1973).

3. See Securities Act Release No. 4924 (Sept. 20, 1968), [1967-1969 Transfer Binder] FED. SEC. L. REP. (CCH) ¶77,606.

4. Panel Discussion, *Public Information Act and Interpretive and Advisory Rulings*, 20 AD. LAW REV. 1, 29 (1967).

it may be lore, l-o-r-e, but it is not law."⁵ In 1970, the SEC adopted a rule providing for the public release of staff no-action letters.⁶ The decision to make these letters available had the effect of transforming them into law, as Mr. Goldwasser's book amply demonstrates. The law in A GUIDE TO RULE 144 is almost entirely the law created by the availability of SEC interpretive letters.

No-action letters are reported on a selective basis in standard securities law looseleaf services.⁷ Over two-thirds of the staff letters cited by Mr. Goldwasser have not been among those so reprinted. Until recently, obtaining access to these publicly released but unpublished letters was a cumbersome task at best. From the acknowledgment in his preface, it would appear that Mr. Goldwasser acquired copies from a broker-friend.⁸ The newly developed capacity for computerized retrieval of all relevant no-action letters through the Lexis system⁹ has opened to greater numbers of lawyers this vast body of law to search and cite. Mr. Goldwasser demonstrates the creative use which can be made of the expanded body of interpretive rulings by alerting readers to the pitfalls which they have exposed in one area.

As with any attempt to synthesize a vast body of law, a danger of overstating the reach of precedent exists. One example of that is Goldwasser's discussion of the treatment of testamentary trusts and their beneficiaries under Rule 144. Generally, under the rule, restricted securities may not be resold unless they have been held for at least two years. An exception to this holding period requirement is made for nonaffiliated estates and nonaffiliated estate beneficiaries. As Mr. Goldwasser indicates, the staff position in *Federation of Protestant Welfare Agencies, Inc.*¹⁰ suggests that the beneficiary of a testamentary trust is subject to the holding period requirements for restricted securities as is any trust beneficiary. He is not treated as the beneficiary of an estate. However, contrary to Goldwasser's statement, the trust, itself, would appear to be treated as an *estate* beneficiary, subject to the more lax requirements for resale by nonaffiliates.¹¹

Goldwasser devotes particular attention to problems of reselling securities which are subject to resale restrictions but do not fall within the Rule 144 definition of "restricted securities." Underwriters' compensation shares, for example, are often acquired as part of a public offering and must be resold by nonaffiliates under a registration statement or under some exemption outside of Rule 144. The staff has, however, per-

5. *Id.*

6. 17 C.F.R. § 200.81, adopted in Securities Act Release No. 5098 (Oct. 29, 1970), [1970-1971 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 77,921.

7. FED. SEC. L. REP. (CCH) and, to a lesser extent, SEC. REG. & L. REP. (BNA) reprint such letters selectively.

8. GOLDWASSER, *supra* note 1, at ix.

9. Mead Data Central Inc.'s computerized legal research system.

10. [1972-1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 79,264.

11. See Pneumatic Scale Corp., available March 3, 1975.

mitted resales outside of Rule 144 on terms very similar to those of sales under the rule.¹² In the situations with which Goldwasser is primarily concerned, failure to come within Rule 144 may impose more onerous resale requirements than falling within the terms of the Rule. Thus, affiliates, in such situations, since any sales by them are covered by the rule, are in the anomalous position of being able to resell such securities more readily than nonaffiliates. Unfortunately, the book devotes only a part of one footnote¹³ to an equally perplexing question: When is a nonaffiliate who purchases in reliance upon the intrastate exemption of Section 3(a)(11) or Rule 147 in a transaction that could also be characterized as a private offering required to resell under the strict requirements of Rule 144 rather than under the more lax requirements of the intrastate exemption provisions? Should lawyers plan small intrastate transactions to include at least one unsophisticated investor in order to assure that the securities escape the "restricted" label? Would the resulting planned inadvertent public offering permit nonaffiliates to avoid Rule 144's coverage?

A number of the interesting suggestions for interpreting and implementing Rule 144 are found throughout A GUIDE TO RULE 144. The model broker's questionnaire and letters for use in carrying out a Rule 144 transaction are valuable aids.¹⁴ Perhaps the most provocative suggestion which Goldwasser advances for interpreting the rule is the expanded use of the attribution rules of 144(a)(2). Since the attribution rules purport to define the term "person," Goldwasser would apply this definition not only to determine what sales must be counted together, but also to determine who is an affiliate, *i.e.* who is a control "person."¹⁵ Thus, a corporate director who, with his family, did not own ten percent of a class of stock would not be an affiliate if he did not dominate and was not dominated by the other members of the board. Such an approach would eliminate the current concept that all members of a "controlling group" are affiliates.¹⁶ While Goldwasser never states this result explicitly, it is the ineluctable result of his thesis.

The reader may have a few quibbles with A GUIDE TO RULE 144. All lawyers who draft registration statements are aware of the danger in a scissors and paste-pot job, *i.e.* in building upon an earlier registration statement, there is the risk that old language, no longer appropriate, may inadvertently be left in the new document.¹⁷ At one point, Goldwasser has apparently succumbed to this kind of danger in preparing a new edition based upon the old. Section 6.03.2.3 discussed language relating

12. GOLDWASSER, *supra* note 1, at 127, 409-11.

13. *Id.* at 154 n.206.

14. *Id.* at 381-402.

15. *Id.* at 97.

16. *Id.* at 96-101.

17. *Cf. Escott v. Bar Chris Construction Co.*, 283 F. Supp. 643, 690 (S.D.N.Y. 1968) (Director's drafting of new prospectus by use of large portions of earlier prospectus resulted in suit against company as a result of false statements and material omissions in new prospectus due to change in circumstances).

to availability of current public information which was removed from the Rule in a 1974 amendment.¹⁸

Elsewhere, a few statements appear inaccurate. For example, Goldwasser indicates that aftermarket prospectus delivery by dealers is required during the relevant time period, "regardless of whether the actual shares being sold were among those in the registered offering."¹⁹ While this statement reflects the practice resulting from the difficulty in tracing certificates in cases where previously issued shares are being traded, and the aftermarket delivery requirement is applicable,²⁰ it does not reflect the legal requirement as interpreted in *Barnes v. Osofsky*.²¹

The need for this second edition of A GUIDE TO RULE 144 only three years after the first suggests the rapidity with which new developments in the area occur. Indeed, only months after the publication of this second edition, major amendments to Rule 144 were promulgated.²² These amendments increased the volume of securities that can be sold under the rule in two ways. First, they reduced the measuring period during which the applicable volume can be sold from six months to three. Second, they permitted the volume of exchange listed and NASDAQ traded securities to be computed as the greater, rather than the lesser, of 1% of the class or the average weekly trading volume. Coupled with this, they permitted securities traded only over-the-counter, but through the facilities of NASDAQ, to use, as an alternative measure of volume, a quantity based upon average weekly trading volume, rather than limiting such over-the-counter securities to a volume based upon 1% of the class.

The new amendments also eliminated an anomaly that had previously existed relating to manner of sale. No longer must the seller interpose a broker between himself and the market maker in order to sell under the rule. Now, not only may securities be sold in unsolicited brokers' transactions, but they may also be sold in transactions directly with a market maker.

Finally, these new amendments further relax the requirements of Rule 144 as applied to sales by nonaffiliated estates and nonaffiliated beneficiaries of estates. Such sellers were already exempted from the holding period and volume requirements of the rule. Now, they are also exempted from the requirements that such sales be made in brokers' transactions or to market makers. Estates and estate beneficiaries (so long as they are not

18. Securities Act Rel. No. 5452 (Feb. 1, 1974), [1973-1974 Transfer Binder] FED. SEC. L. REP. (CCH) ¶79,663, reprinted as Appendix H in GOLDWASSER, *supra* note 1, at 533.

19. GOLDWASSER, *supra* note 1, at 411.

20. Rule 174 under the Securities Act of 1933 excuses after-market prospectus delivery by dealers who have distributed their original allotment of securities and are not acting as underwriters where the issuer was publicly held (i.e., reporting under the Exchange Act) prior to the registered offering.

21. 373 F.2d 269 (2d Cir. 1967).

22. Securities Act Release No. 5979 (Sept. 19, 1978), [1978 Transfer Binder] FED. SEC. L. REP. ¶81,731; Securities Act Release No. 5998 (Nov. 8, 1978), [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶81,759.

affiliates of the issuer) may now sell to purchasers who have been solicited to buy, as long as the current public information and filing requirements of the rule are met.

More recently, additional amendments to the rule were promulgated.²³ These amendments entirely eliminated the volume limits for nonaffiliates who have owned exchange or NASDAQ-listed securities for three years or who have owned other securities registered under Section 12 of the Exchange Act for four years. Sellers must have been nonaffiliates for at least three months prior to the sale to take advantage of these new provisions.

The new changes will no doubt create many new interpretive problems. For their resolution, one eagerly looks forward to a third edition by Dan Goldwasser.

23. Securities Act Release No. 6032 (March 5, 1979), [Current Binder] FED. SEC. L. REP. (CCH) ¶ 81,992.