FEINSTEIN LAW

CORPORATE & SECURITIES COUNSEL

January 8, 2021

John Fieldsend
Sean Harrison
Office of Rulemaking
Division of Corporation Finance
U.S. Securities and Exchange Commission
100 F Street NE Washington, DC 20549
VIA ELECTRONIC MAIL

Re: Release Nos. 33-10911; 34-90773; File No. S7-24-20

Dear Mr. Fieldsend and Mr. Harrison:

We appreciate the opportunity to comment on the Securities and Exchange Commission's proposed amendment to Rule 144 (*Release Nos. 33-10911; 34-90773; File No. S7-24-20*). For the reasons listed below, we believe the Commission should find alternative methods to achieve its stated goals.

Question 1 asks if the SEC *should amend Rule 144(d)(3)(ii) as proposed?*

We do not believe the SEC should amend rule 144 as proposed. We believe such an amendment would shut down an essential industry for which there is a clear and defined role in well-functioning capital markets. Furthermore, the proposal is not likely to achieve its stated goal. Rather than reducing unregistered distributions, the proposed amendment would merely create another level of 'whack-a-mole' for SEC regulators, with securities lawyers quickly coming up with new transactional tools and capital structures that remain outside the purview of the amended language; we've already seen several innovative structures created in anticipation of the new rules.

We are also concerned that the proposal's rationale for disallowing the holders of market-adjustable convertible notes availing themselves of tacking under Rule 144 – that such securities are not subject to the risks of loss inherent in other kinds of restricted securities that may tack for the purposes of a Rule 144 transaction – is conclusory and inaccurate. Investors in market-adjustable convertible notes very frequently suffer partial or complete loss of their investment due to an issuer's refusal or inability to pay off a note or deliver the shares due thereunder. This is true whether by the issuer's aggressive denials, ghosting, declaration of bankruptcy, filing of often frivolous and far-fetched counterclaims,

interpleader, and attempts to characterize the transactions as usurious loans. Footnote 26 to the proposal explains the purported lack of the risks of loss of these kinds of investment because *"this risk is borne for a briefer duration currently than when Rule 144 was originally adopted because of the shortened holding periods."* We struggle to understand the relevance of the shortened period to the very real risks facing convertible note investors that they may fail to recover from companies the value of their investment or any value at all from conversion shares.

If the SEC or another agency have data supporting the assertion that the risks of this kind of investment are far lower than other investments for which Rule 144 tacking is available, this could help the discussion and build acceptance of the proposed amendment. In lieu of such data, we question the accuracy of this assumption.

Rather than adding another Rule 144 requirement to be enforced within a scattershot framework of attorney opinion mills, SEC 'no action' letters, and arbitrary and inconsistently applied legal standards set forth by a diverse set of tribunals, we support mandatory, strict disclosure requirements in connection with any securities transaction that may have actual and possible future material effects on the structure and dilution of the company's stock. Furthermore, we support the Commission's study of additional mandatory disclosure requirements that will help accomplish the stated goals of the proposed amendments.

Question 2-5 ask about the definitions of market-adjustable securities and whether listed companies should also be subject to the amended rule.

Whether the issuer is listed or unlisted and whether a market-adjusted security is involved is irrelevant. We believe that the sales of any security, including convertible notes, should be fully and accurately disclosed by companies in a fully transparent manner that allows the market to accurately evaluate all material consequences of such transactions. These financing transactions are a regular and essential part of the functioning small-cap market and should be permitted with robust disclosures that allow the public to view the true dilution – both actual and potential - and for which the issuer and lender remain accountable.

Question 6 asks if there are alternative approaches that we should consider that would better mitigate the risk of unregistered distributions of securities acquired upon the conversion or exchange of market-adjustable securities?

The approach we favor mitigates the risk to existing shareholders of unregistered distributions of securities by fully informing those shareholders of those risks and all possible consequences of the distribution both at the time of the conversion as well as *at the time the original convertible note is sold*. The Commission already requires filings by both listed and unlisted companies when they sell securities under Reg D exemptions; why not create a mandatory disclosure form for companies when they sell convertible notes? A standardized, thoughtful set of disclosure requirements would include a table of all possible dilutive scenarios and would mitigate the risks to existing and prospective investors while reducing the number of transactions that don't 'pass the smell test.' It would also provide a database that could prove valuable to regulators seeking out unregistered brokers and dealers. Initially aggressive enforcement of the veracity and sufficiency of such disclosures under existing anti-fraud

provisions of federal and state law should be prioritized by regulators if the Commission chose this solution.

We believe another factor that must be addressed when discussing the reduction of unregistered distributions by holders of market-adjusted convertible notes: Bad actors. We represent transfer agents plagued by a constant stream of characters trying to inappropriately remove legends using the full litany of well-worn tools: round trips, gypsy swaps, 4(a)(1) opinions that don't comport with regulations, conclusory attorney opinions from non-attorneys, unlicensed attorneys, or 'opinion mills', dilution scams existing for no other reason that executives lining their pockets, and a dozen other clever and no-so-clever ruses – all with the goal of selling cheap paper quickly. The purveyors of these documents are well known to transfer agents, and many of them are repeat players.

If the Commission intends, as it has repeatedly stated, for transfer agents to help reduce unregistered distributions as one of their 'gatekeeper' duties, it should supply the agents with additional tools under the authority granted in Section 17A(a)(2)(A)(ii) of the Securities Exchange Act of 1934 to allow those transfer agents to work with the Commission to reduce the improper removal of legends and the distributions that flow therefrom. It is true that transfer agents can and do use FinCEN's Suspicious Activity Reporting System (SARS) to report certain financial transactions, but SARS is designed to combat money laundering, not sketchy legend removals. No analogous system exists to easily report to the Commission suspected scalpers, undisclosed paying promoters, bad opinion writers, improper converters, material misrepresenters, and perpetrators of other suspicious securities transactions. If such a system existed, it could provide Commission regulators with the information they need to expose existing networks of unscrupulous players who take advantage of the lack of coordination between regulators and the transfer agent industry to invalidly remove legends and sell securities.

Finally, we note that the Commission has recently shown a willingness to try to control unregistered distributions via expanding the definition of "dealer" in enforcement actions against prominent convertible note investors. In a line of cases that began with *S.E.C. v. Big Apple Consulting USA, Inc., 783 F.3d 786, 809 (11th Cir. 2015)* and continued through recent actions against *Ibrahim Almagarby, et al. (No. 17-cv-62255), Justin Keener/JMJ Partners, John Fierro/JDF Capital, and John Fife/Chicago Venture Partners,* the Commission argues that these convertible note buyers are unregistered dealers *"in the business of buying and selling securities."* In our opinion, the test of who is 'in the business' is convoluted and imprecise, leaving regulation and enforcement over parties to these types of transactions to an uncertain, *ad-hoc* determination that encroaches on a CEO's ability to make business decisions that lead to the formation of capital. The instant proposal shares a similar goal to these enforcement actions and appears to be targeted at the same holders of market-adjustable convertible notes as the above-described enforcement actions. We would encourage the Commission to take on the matter directly, rather than via ad-hoc litigation or rule amendments with indirect and avoidable effects.

Questions 7 and 8 ask whether the amended rules should apply to companies with a class of stock listed on a national exchange.

The theory behind this distinction is that national exchanges typically require shareholder approval for transactions that reach a specific level of dilution, which should mitigate the risk to investors. This theory would only be accurate if such disclosures were required to include a more comprehensive

explanation of the transaction than they currently do, including a table setting forth the range of dilution possible under all likely scenarios.

Question 9 asks for any additional amendments or changes to the proposed amendments that the SEC should consider that would help achieve the purposes of the proposal?

The proposed amendments to Rule 144 state that their purpose is to reduce or mitigate the risk of unregistered distributions of securities to the investing public. This is a laudable goal, but the proposal fails to account for one important fact that will never change: As long as there is a single corporate CEO with no cash and a desire to see his business dream realized, there will be someone out there willing to lend that CEO money in exchange for discounted paper. We believe the approaches we recommend – robust mandatory disclosures of convertible note transactions, collaborative reporting between transfer agents and the Commission, and clear definition by the Commission of 'broker' and 'dealer' for the registration requirements of Section 15(a)(1) of the Securities Exchange Act of 1934 – could significantly reduce both unregistered distributions and distributions by unlicensed brokers and dealers.

A cautionary note: Any rules intending to reduce distributions flowing from conversion of market-adjustable securities recognize the need for CEOs to have freedom in their business decisions and should avoid creating a significant burden to their ability to strike a bargain with qualified investors that will lead to capital formation for the company and return on investment for the investor.

The Feinstein Law Firm counsels transfer agents, emerging markets issuers, broker/dealers, private investors, and other stakeholders who may be impacted by the proposed amendments. We formed these comments after consultation with a number of interested clients, and we appreciate their input. For more information, please visit www.feinsteinlawfirm.com