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SEC Interprets Section 3(a)(10) Exemption from Registration Requirements of the Securities Act of 1933 and Resale Status of Securities that are Received in Section 3(a)(10) Exempt Transactions

The Division of Corporation Finance (the "Division") of the Securities and Exchange Commission (the "Commission") recently issued a legal bulletin expressing its views regarding the resale status of securities received in a transaction exempt from registration pursuant to Section 3(a)(10) of the Securities Act of 1933.[1] This memorandum summarizes the SEC's views on the Section 3(a)(10) exemption and the resale status of securities received in such an exempt transaction.

I. EXEMPTION FROM SECURITIES ACT REGISTRATION UNDER SECTION 3(a)(10) OF THE SECURITIES ACT OF 1933

Section 3(a)(10) of the Securities Act of 1933[2] is an exemption from Securities Act registration for offers and sales of securities in specified exchange transactions, the terms and conditions of which a court or authorized governmental entity[3] has approved, after holding a hearing, as fair to those to whom the securities will be issued.[4] The Section 3(a)(10) exemption is available without any action by the

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1 Division of Corporation Finance, Securities and Exchange Commission, Staff Legal Bulletin No. 3A (CF), June 18, 2008.

2 "Sec. 3(a) Except as hereinafter expressly provided the provisions of this title shall not apply to any of the following classes of securities. ***

(10) Except with respect to a security exchanged in a case under title 11 of the United States Code, any security which is issued in exchange for one or more bona fide outstanding securities, claims or property interests, or partly in such exchange and partly for cash, where the terms and conditions of such issuance and exchange are approved, after a hearing upon the fairness of such terms and conditions at which all persons to whom it is proposed to issue securities in such exchange shall have the right to appear, by any court, or by any official or agency of the United States, or by any State or Territorial banking or insurance commission or other governmental authority expressly authorized by law to grant such approval."

15 U.S.C. §77c(a)(10).

3 Authorized governmental entities may include state insurance commissions, state corporation or securities commissions, state banking agencies, etc.

4 Note, however, that securities that are exempt from registration under Section 3(a)(10) are not exempt from the registration or qualification provisions of any state securities laws, for they are not "covered securities" under Section 18 of the Securities Act. See Section 18(a)(4)(C).

Division or the Commission. However, the issuer must advise the court or authorized governmental entity before the fairness hearing that it will rely on the Section 3(a)(10) exemption upon the court or authorized governmental entity's approval of the exchange. In addition, the issuer must provide the court or authorized governmental entity with sufficient information to determine the value of both the securities claims or interests to be surrendered and the securities to be issued in the proposed transaction. Finally, the issuer must provide timely and appropriate notice of the hearing to all persons who will receive securities in the proposed exchange.[5]

Issuers that are unsure of whether the exemption is available for a specific contemplated transaction may, however, seek the Division's views by requesting a "no-action" position from the Division. An issuer must submit a no-action request *before* the fairness hearing,[6] for the Division will not issue a no-action response concerning a transaction after the fairness hearing has been held.

Section 3(a)(10) Exchange Transactions

In order to qualify for exemption from registration under Section 3(a)(10), securities must be issued in exchange for securities, claims, or property interests; they cannot be offered for cash. This requirement generally does not raise interpretive issues. However, it is important to note that when options, warrants, or other convertible securities are issued in a Section 3(a)(10) transaction, Section 3(a)(10) does not exempt a later exercise or conversion.

Fairness Hearings

A court or authorized governmental entity must hold a hearing that is open to all those who will receive securities in the proposed exchange and find that the proposed exchange's terms and conditions are fair to all such persons. If a governmental entity is approving the exchange, that entity must be authorized by statute to (1) hold a hearing on the transaction (though the statute need not require the hearing), and (2) affirmatively conclude that the exchange is fair to the security holders participating in the exchange.[7] Under the Division's interpretation, the term "any court" in Section 3(a)(10) may include a foreign court. Regarding no-action requests in transactions to be approved by a foreign court, all requirements that apply to exchanges approved by a U.S. court must be met; in addition, the issuer must provide the Division with an opinion from counsel licensed to practice in the foreign jurisdiction stating that approval by the foreign court is contingent on prior approval of the fairness of the proposed exchange to persons receiving securities in the exchange.

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5 The anti-fraud requirements of the federal securities laws govern disclosure. However, Section 3(a)(10) does not specify the information that must be included in the required notice. Therefore, the Division, in connection with no-action requests, will consider only whether the issuer's notice adequately (1) advises the persons to receive securities in the exchange of their right to attend the hearing and (2) gives the information necessary to exercise that right.

6 Generally, the Division strives to respond to requests for no-action within 30 days of receipt.

7 When the governmental entity's statutory authority is unclear, actual practice of that entity may provide guidance. For example, in State Mutual Life Assurance Company (Mar. 23, 1995), the Division relied on an opinion from counsel to the Division of Insurance of the Commonwealth of Massachusetts that the relevant statute authorized the Massachusetts Insurance Commissioner to make the requisite fairness determination.

II. RESALE STATUS OF SECURITIES RECEIVED IN 3(a)(10) EXEMPT TRANSACTION

It is the Division's view that, in light of Securities Act Release No. 8869 (Dec. 6, 2007)[8], securities received in a Rule 145(a) reclassification, merger or consolidation, or transfer of assets that does not involve a shell company and is exempt under Section 3(a)(10) are not "restricted securities" and may generally be resold without regard to the Rule 144 safe harbor, if the sellers are not affiliates of the issuer of the Section 3(a)(10) securities and have not been affiliates within 90 days of the date of the Section 3(a)(10) exempt transaction. By contrast, if the securities are held by affiliates of the issuer, those holders may be able to resell the securities in accordance with the provisions of Rule 144.

When a Rule 145(a) transaction does involve a shell company, other than a business combination related shell company, and is exempt under Section 3(a)(10), then the Rule 145(c) and (d) resale limitations apply to any party to that transaction (other than the issuer of the Section 3(a)(10) securities) and to any person who is an affiliate of such party at the time such transaction is submitted for vote or consent.

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Charles A. Gilman at (212) 701-3403 or cgilman@cahill.com; Jon Mark at (212) 701-3100 or jmark@cahill.com; John Schuster at (212) 701-3323 or jschuster@cahill.com.

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8 Securities Act Release No. 8869 (Dec. 6, 2007) amended, among other things, Securities Act Rule 145 to eliminate the presumptive underwriter provision in Rule 145(c) except for transactions involving a shell company, other than a business combination related shell company.