

[Securities Regulation Daily Wrap Up, TOP STORY—SEC modernizes adviser marketing rules, proposes closing Rule 144 loophole for market-adjustable securities, \(Dec. 22, 2020\)](#)

Securities Regulation Daily Wrap Up

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The SEC's new merged rule on adviser marketing communications replaces rules on advertising and cash solicitation that were adopted in 1961 and 1979, respectively, while the Rule 144 proposal seeks to ensure that holders of market-adjustable securities are not acting as conduits for unregistered sales.

Rules that govern investment adviser advertisements and payments to solicitors are set to be modernized now that the SEC has finalized reforms under the Advisers Act. The amendments reduce the existing rules to a single rule designed to prevent fraud and provide investors with the information necessary to make informed decisions in choosing investment advisers and advisory services (*Investment Adviser Marketing*, [Release No. IA-5653](#), December 22, 2020).

Separately, the SEC has proposed to amend Securities Act Rule 144 to revise the holding period determination for securities acquired upon the conversion or exchange of certain "market-adjustable securities." The proposed amendment seeks to close a loophole and reduce the risk of unregistered distributions in Rule 144 sales of these securities by mandating that the required holding period under the rule would not begin until the securities are acquired upon the conversion or exchange of the market-adjustable security. The Commission also voted to propose amendments to update and simplify the Form 144 filing requirements (*Rule 144 Holding Period and Form 144 Filings*, [Release No. 33-10911](#), December 22, 2020).

Adviser marketing. The [new single rule](#) adopted by the SEC, designed to regulate investment advisers' marketing communications, will replace the current advertising and cash solicitation rules, Advisers Act Rule 206(4)-1 and Rule 206(4)-3. Related amendments were also made to Rule 204-2, the books and records rule, and Form ADV, the investment adviser registration form. Third-party ratings included in advertisements will require specific disclosures to prevent them from being misleading while testimonials and endorsements will be permitted, subject to certain conditions. No-action letters and other guidance addressing the advertising and cash solicitation rules will be withdrawn if they no longer apply or are incorporated into the final rule.

Specifically, the amended definition of "advertisement" captures traditional communication covered by the advertising rule and solicitation activities covered by the previous cash solicitation rule. Prohibited advertising practices include those that are materially false or misleading, statements which the adviser does not have a reasonable basis for believing, or investment advice that is not presented in a fair and balanced manner. Among other things, the rule also prohibits advertisements which include certain performance metrics if corresponding information is not provided as well.

"The marketing rule reflects important updates to the traditional advertising and solicitation regimes, which have not been amended for decades, despite our evolving financial markets and technology," said Chairman Jay Clayton. "This comprehensive framework for regulating advisers' marketing communications recognizes the increasing use of electronic media and mobile communications and will serve to improve the quality of information available to investors. The new rule provides for an extended compliance period intended to provide advisers with a sufficient transition period, including to enable consultation with the Commission's expert staff."

Effective date. The amendments will be effective 60 days after publication in the *Federal Register*. Advisers will have 18 months after the effective date to comply with the amendments.

Rule 144 holding period. Securities Act Rule 144 provides a non-exclusive safe harbor from the statutory definition of "underwriter" to assist security holders in determining whether the registration exemption under Securities Act Section 4(a)(1) is available for the resale of restricted or control securities. One of the conditions under Rule 144 is that a selling security holder must have held the securities for a specified period of time prior to resale, either six months for securities of an issuer that has been a reporting company for at least 90 days or one year for securities issued by a non-reporting company.

Rule 144 does contain "tacking" provisions in specified situations, however, to allow holders to count other holding periods, including certain sales of convertible securities. Rule 144(d)(3)(ii) currently allows securities acquired solely in exchange for other securities of the same issuer to be deemed to have been acquired at the same time as the securities surrendered for conversion or exchange. As a result, after the Rule 144 holding period has been satisfied, holders of market-adjustable securities can convert them and quickly sell the underlying securities into the public market, creating an incentive to purchase market-adjustable securities with a view to distributing the underlying securities to capture the difference between the built-in discount and the market value of the underlying securities.

To reduce this risk, the SEC has proposed to amend Rule 144(d)(3)(ii) to eliminate tacking for certain securities acquired upon the conversion or exchange of the market-adjustable securities. As a result, the holding period for the underlying securities would not begin until the conversion or exchange of the market-adjustable securities. The proposed amendment would only apply, however, to market-adjustable securities transactions in which:

1. The newly acquired securities were acquired from an issuer that, at the time of the conversion or exchange, does not have a class of securities listed, or approved for listing, on a registered national securities exchange; and
2. The convertible or exchangeable security contains terms, such as conversion rate or price adjustments, that wholly or partially offset declines in the market value of the underlying securities occurring prior to conversion or exchange, other than terms that adjust for stock splits, dividends, or other issuer-initiated changes in its capitalization.

"Today's proposed amendments modernize, clarify and strengthen Rule 144, including to ensure that holders of market-adjustable securities are assuming the economic risks of their investment rather than acting as a conduit for an unregistered sale of securities to the public on behalf of an issuer," said SEC Chairman Jay Clayton in a [news release](#).

Forms 4, 5, and 144 filing requirements. The SEC's proposal would also mandate electronic filing of Form 144, eliminate the requirement to file a Form 144 with respect to sales of securities issued by companies that are not subject to Exchange Act reporting, and amend the Form 144 filing deadline to coincide with the Form 4 filing deadline. The proposal would also amend Forms 4 and 5 to add an optional check box to indicate that a reported transaction was intended to satisfy Exchange Act Rule 10b5-1(c), which provides an affirmative defense for trading on the basis of material non-public information in insider trading cases.

Comment period. The public comment period on the Rule 144 proposal will remain open for 60 days following publication of the proposing release in the *Federal Register*.

The releases are [No. IA-5653](#) (*Investment Adviser Marketing*) and [No. 33-10911](#) (*Rule 144 Holding Period and Form 144 Filings*).

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