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DTC Eligibility and DTC Chills

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DTC Eligibility, DTC Chills And Global Locks For OTC Markets Companies- In the first LawCast in this series I discussed generally what the DTC is and the basic eligibility requirements. Today I will discuss “chills” and “global locks.”

Many OTC Issuers have faced a “DTC chill” without understanding what it is, let alone how to correct the problem. A DTC chill is the suspension of certain DTC services with respect to a company’s securities. Those services can be book entry clearing and settlement services, deposit services or withdrawal services. A chill can pertain to one or all of these services. In the case of a chill on all services, it is called a “Global Lock.”

From the DTC’s perspective, a chill does not change the eligibility status of a company’s securities, just what services the DTC will offer for those securities. For example, the DTC can refuse to allow further securities to be deposited into the DTC system or can refuse to allow the book entry trading and settlement of those securities.

Although I’m sure it’s unintentional, the term “chill” speaks volumes as to the reality of the effects of a DTC chill. A DTC chill results in a chilling of trading in a security, a chilling of any financing transactions, and a chilling of potential reverse or forward acquisitions or mergers.

As a result of a complex layer of laws involving many issues including privity between a public company and DTC and considerations related to governmental and quasi-governmental regulatory organizations, for many years DTC refused to have any direct dealings with companies even though the imposition of a chill or global lock had a significant direct impact on such company.

On March 15, 2012 the SEC issued an administrative opinion stating that a company is entitled to due process and fair proceedings by DTC as a result of a DTC chill placed on that company's securities. The SEC held that a company is entitled to advance notice and opportunity to address or cure an issue prior to the imposition of a chill, provided, that DTC could still impose a chill without notice in an emergency situation such as where there is clear ineligibility and a continuous violation in process.

Immediately following the SEC ruling, DTC began changing its process and procedures for dealing with companies. Twice DTC published proposed rules and then withdrew them and in practice, its

procedures for dealing with chills evolved fairly constantly over a period of a couple of years, with each evolution making the process more efficient and standardized for companies and legal practitioners assisting clients in resolving chills and locks such as my firm.

To simplify a complicated issue – at the end of the day, a DTC chill is resolved by a legal opinion letter confirming the free tradeability of shares in the DTC system and the existence of freely tradeable shares held by shareholders that are, or will become, eligible to be deposited into the DTC system.

To prepare such a letter an attorney must review the underlying paperwork and legal basis for prior deposits into the DTC system and confirm the continued eligibility of the company's shareholders to rely on Rule 144. So, for example, if the company is a shell, or a former shell that is delinquent in its SEC reporting requirements, its shareholders would not be able to rely on Rule 144 and continued DTC eligibility would be problematic.

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Securities attorney Laura Anthony and her experienced legal team provides ongoing corporate counsel to small and mid-size OTC issuers as well as private companies going public on the over-the-counter market, such as the OTCBB, OTCQB and OTCQX. For nearly two decades Legal & Compliance, LLC has served as the “Big Firm Alternative.” Clients receive fast, personalized, cutting-edge legal service without the inherent delays and unnecessary expenses associated with “partner-heavy” securities law firms. The firm’s focus includes, but is not limited to, registration statements, including Forms 10, S-1, S-8 and S-4, compliance with the reporting requirements of the Securities Exchange Act of 1934, including Forms 10-Q, 10-K and 8-K, 14C Information Statements and 14A Proxy Statements, going public transactions, mergers and acquisitions including both reverse mergers and forward mergers, private placements, PIPE transactions, Regulation A offerings, and crowdfunding. Moreover, Ms. Anthony and her firm represents both target and acquiring companies in reverse mergers and forward mergers, including the preparation of transaction documents such as Merger Agreements, Share Exchange Agreements, Stock Purchase Agreements, Asset Purchase Agreements and Reorganization Agreements. Ms. Anthony’s legal team prepares the necessary documentation and assists in completing the requirements of federal and state securities laws and SROs such as FINRA and DTC for 15c2-11 applications, corporate name changes, reverse and forward splits and changes of domicile. In addition to many other major metropolitan areas, the firm currently represents clients in New York, Las Vegas, Los Angeles, Miami, Boca Raton, West Palm Beach, Atlanta, Phoenix, Scottsdale, Charlotte, Cincinnati, Cleveland, Washington D.C., Denver, Tampa, Detroit and Dallas.

Ms. Anthony is the author of SecuritiesLawBlog.com, the OTC Market’s top source for industry news Industry’s news, and the producer and host of LawCast.com, the securities law network. Ms. Anthony is a member of; Cystic Fibrosis Foundation Arthur’s Jam event committee; the Society of the Four Arts Contemporaries, Young Friends of the Norton Museum of Art, Palm Beach County Zoo Society, Kravis Center for the Performing Arts, the Crowdfunding Professional Association (CfPA), Palm Beach County Bar Association, the Florida Bar Association, the American Bar Association and the ABA committee on Federal Securities Regulations. She currently resides in West Palm Beach with her husband and daughter.

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