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MEMORANDUM

To: All Clients

Re: Becoming a Publicly Trading Company – Reverse Mergers and Self-Registrations

About Reverse Mergers

A Reverse Merger is a transaction where by a private company becomes a public company by merging with a public shell company. A shell company is a company that has substantially no assets, except its corporate structure. A Company can become a shell company by agreeing to spin off its current assets and liabilities at the time of the merger. Upon the merger, the private company shareholders receive a substantial majority of the shares of the public company (normally 90% to 95% or perhaps more) and the control of the board of directors, resulting in the private company becoming an operating public company. Prior to the merger, the transaction does not go through a review process with state and federal regulators. The transaction involves the private and shell company exchanging information on each other, negotiating the merger terms, and signing a share exchange agreement. At the closing, the public shell company issues a substantial majority of its shares and the board control to the shareholders of the private company. In return for the sale of the shell, the private company pays the shareholders of the public shell company a sum of money and the shareholders of the public shell retain a negotiated amount of shares of stock in the combined company. The amount of money and percentage of shares retained is a matter of negotiation between the parties. It depends upon the (i) value of private operating company (ii) type of shell (reporting, not reporting and which exchange it is on) and (iii) what the parties want (somewhat more money and less stock, others want less money and more stock.)

As in the Self-Registration process, there are **four (4) prerequisites** that the Company needs to meet in order to raise money by publicly selling shares of its stock.

The four requirements are:

1. The Company must have at least 40 shareholders (preferably 50 to 60) holding at least 100 shares each in order to be considered a publicly company.
2. The shares of stock that these shareholders hold must be “freely trading.”
3. The Company is a SEC reporting company, subject to the Securities Exchange Act of 1934 and up to date with its filing requirements.
4. The Company is listed on an Exchange, including the OTC Bulletin Board.

In some cases, the public shell company would have already met all of these requirements before the merger. If all the requirements are already met, the Company is a public trading company immediately and can begin to raise money by publicly selling additional shares of its stock upon the filing of a new registration statement with the SEC. In other cases, the public shell company did not meet these four requirements before the merger. In that case, after the merge, the Company will have to meet those requirements prior to publicly selling additional new shares. In both such situations the exchange will require the combined company to show that it meets the initial listing requirements for that exchange.

Plan of Action for a Reverse Merger

Identify a suitable shell company. Public shell companies come in all shapes and sizes. As previously stated, some shell companies have met the four criteria stated above; while others may have met only two of the four. Some are listed on the OTCBB or NASDAQ, while others may be listed on the Pink Sheets. An even more important distinction is whether the shell company is “clean” or not. Some qualities that make a shell company “not clean” are: (i) directors/officers/shareholders of the shell having violated “bad boy” provisions of federal or state securities law or (ii) the shell company is vulnerable to lawsuits from potential plaintiffs, (iii) having potential liabilities (iv) not being current of 34 Act filings, (v) not having voting controls of the Company and (vi) not having enough authorized shares available to issue

Negotiate an Agreement. The private company and the shell company must negotiate and finalize a deal. This is often a more time-consuming process than expected.

Conduct due diligence. Once a suitable shell company is found, due diligence must be conducted. The history of the shell company, its shareholders, and its officers/directors must be documented and reviewed to ensure a smooth merger.

Effecting a Merger. All the transactions associated with a merger must be completed by shareholders on both sides of the deal.

Post Merger Filing Requirements. Four business days, and preferably as early as possible after the closing of the reverse merger, the newly-merged company (the “Company”) must file a Current Report on Form 8-K with the SEC, along with audited financials, of the operating company. The 8-K describes the newly combined company, stock issued, information on the new officers and directors, a full description of the business, and financial statements audited to US GAAP standards. The 8-K must disclose substantially similar type of information that it would be required to provide in registering a class of securities under the Securities Exchange Act of 1934 (see discussion below). Also the Company will need to continue its reporting requirements with the SEC.

Post Merger Transactions. If the public shell with which the Company has merged into did not meet the four requirements stated above, then the Company will need to meet those requirements after the merger.

About Self Registration

Self Registration is an alternative method to raise funds and become a public company without the services of an investment banking firm. In this method, your private company raises money in a private placement by selling unregistered shares to “accredited investors” and at the same time agreeing to register such shares by filing a registration statement on Form S-1 (or for Foreign Companies, Form F-1) or SB-2 with the Securities and Exchange Commission. The private placement is then done. After that registration statement is prepared, filed with the SEC and declared effective, the holders of the shares purchased in the Private Placement may sell the shares publicly on an exchange if the Company is listed on an exchange. After the Registration Statement is first filed with the SEC, the SEC will generally review the Registration Statement and provide comments within 30 days. The Company will then address comments to the filing issued by the Commission and amend the filing in response thereto. After the comments are successfully responded to, the Commission will declare the registration statement effective.

The Registration Statement consists of a narrative description of the Company, its Business, Management, Risk Factors and a description of the securities and the Plan of Distribution and Audited financial statements for the past 2 years (or inception, whichever is less) and stub periods. The registration statement serves multiple purposes. First, it allows the holders of the Company’s securities to sell their shares without further restrictions and second, by filing a Form 8-A at the time the Registration Statement is declared effective, your company makes itself subject to the reporting requirements of the Securities Exchange Act of 1934 (the “’34 Act”). The ’34 Act requires the filing of quarterly reports, annual reports, makes an issuer subject to the proxy rules, and makes your company’s management team subject to Section 16 filings, among other things. Before any stock exchange will list an issuer's common stock, your company must be subject to the reporting requirements of the ’34 Act.

Plan of Action for a Self-Registration

Before any stock exchange will list an issuer's common stock for trading, a company must meet the same four requirements stated above. Because of this requirement, it may be necessary for your company to conduct a private placement to raise money, and issue stock to increase its number of shareholders. The filing of the Registration Statement allows the registered shares to be freely tradable. The filing of the Form 8A then makes the Company subject to the ’34 Act.

In order for a Company to be listed on the Over the Counter Bulletin Board (“OTCBB”), a recommended exchange, a market maker (Broker-Dealer) must file a Form 211 and act as a market maker for your stock. The Market Maker will provide the bid and ask prices for an orderly market. Once your stock is trading, you will be able to raise additional money by selling additional shares of your Company through an underwritten offering or a self-directed offering by the Company by filing another Registration Statement covering such new shares. Subsequent Registration Statements are easier since the SEC already commented on the first one. Furthermore, you are able to raise more money this way since investors would more likely want to invest in a Company that already has a liquid market for its stock so that they could have an exit strategy for this investment.

Differences between a Reverse Merger and a Self-Registration

Advantages of Reverse Merger versus Self-Registration

- The reverse merger process generally takes about 1 month less than self registration.
- The Company will be a publicly-traded company immediately after merger if the shell was previously trading and will not have to wait until SEC clearance
- A suitable shell company will already have the adequate number of Shareholders and freely trading shares.

Disadvantages of Reverse Merger versus Self-Registration

- The costs of buying a shell (up to \$500,000 and up to 10% of your Company) and conducting due diligence can be costly. Furthermore, it is our experience that in many instances the shell company has problems that do not become evident until the due diligence process is completed, at which point a lot of time was wasted.