UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
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OFFICE OF THE
GENERAL COUNSEL

October 29, 2021

The Honorable Vice Chancellor J. Travis Laster
Delaware Court of Chancery
Leonard L. Williams Justice Center
500 North King Street
Wilmington, DE 19801

RE: *In re Forum Mobile, Inc.,* C.A. No. 2020-0346-JTL

Dear Vice-Chancellor Laster:

In response to the Court's opinion of March 18, 2021, and the request of the *amicus curiae* that the Court appointed (Mark Gentile), the Securities and Exchange Commission submits this letter brief offering the following views about the effect of the federal securities laws on the petition filed by Synergy Management Group LLC, which seeks to revive Forum Mobile, Inc., a defunct Delaware company, for possible use in a reverse merger. Forum Mobile is a non-reporting issuer for which little information is publicly available at the moment. We take no position on whether the petition should be granted pursuant to Delaware law.

In a reverse merger, a private company merges with and into a publicly traded entity to obtain access to the capital markets without engaging in a more traditional method of capital formation, such as an initial public offering. Reverse mergers are not per se illegal under the federal securities laws. But when reverse mergers involve non-reporting issuers that are not required to file periodic reports or other information with the Commission, the lack of current and public information may pose a significant risk to investors "because it may prevent them from estimating return probabilities and generative positive returns" and "can contribute to incidents of fraud and manipulation by preventing retail investors from being able to counteract misinformation." *Publication or Submission of Quotations without Specified Information*, 85 Fed. Reg. 68124, 68125 (Oct. 27, 2020); *see also* Joshua T. White, SEC Division of Economic and Risk Analysis, *Outcomes of Investing in OTC Stocks*, at 8-12 (Dec. 16, 2016), *available at* https://www.sec.gov/files/White_OutcomesOTCinvesting.pdf ("*OTC Outcomes*") (reviewing empirical studies showing that lack of information about such issuers is associated with illiquidity, negative returns, and fraud). Indeed, non-reporting issuers have been "frequent targets of market manipulation," including pump-and-dump schemes where insiders tout stock or otherwise illicitly inflate prices of the thinly traded securities so that they may sell their shares for a profit. *OTC Outcomes* at 11-12; Douglas J. Cumming & Sofia Johan, *Listing Standards and Fraud*, 34 Managerial & Decision Econ. 45 (2013); Rajesh Aggarwal & Guojun Wu, *Stock Market Manipulations*, 79 J. Bus. 1915 (2006).

As a consequence of their association with fraudulent and manipulative schemes, these types of reverse mergers have prompted Commission action. The Commission has pursued numerous enforcement actions against defendants who have engaged in fraud in connection with reverse mergers involving non-reporting issuers, including in response to pump-and-dump schemes and other attempts to manipulate the markets. Moreover, the Commission has promulgated several rules as a means to prevent fraud and manipulation that can arise because of the absence of current information about such issuers.

BACKGROUND

Synergy Management Group LLC seeks appointment of its President, Benjamin Berry, as the custodian of Forum Mobile, Inc. Pet. 1. According to Synergy's petition, Forum was incorporated in Delaware in June 1995, but has failed to comply with Delaware law and has abandoned its business. Pet. 2. Synergy states that it owns nearly 500,000 shares of Forum stock. *Id.*

Forum is not a reporting issuer under the Securities Exchange Act of 1934 (Exchange Act), which means it is not required by law to file with the Commission periodic financial reports or other information regarding its business, management, and ownership. Under Section 12(a) of the Exchange Act, 15 U.S.C. 78*l*(a), issuers that want their securities to trade on a national securities exchange, such as the New York Stock Exchange or Nasdaq, must register the securities with the Commission, which triggers periodic and current reporting requirements under Section 13 of the Exchange Act, 15 U.S.C. 78m. Section 12(g) of the Exchange Act also imposes a registration requirement on equity securities. 15 U.S.C. 78*l*(g). Amended by Congress in 2012, Section 12(g) requires an issuer to register its securities—and consequently be subject to reporting requirements—if it has assets exceeding $10 million and a class of equity securities held by 2,000 or more persons, or 500 persons who are not accredited investors (a term defined by the Commission). 15 U.S.C. 78*l*(g)(1)(A), amended by Jumpstart Our Business Startups Act, Pub. L. No. 112-106, § 501, 126 Stat. 306, 326 (2012). Finally, under Section 15(d), issuers are subject to ongoing reporting requirements if they have offered and sold securities pursuant to an effective registration statement (under the Securities Act of 1933) even if they are not required to register their securities under the Exchange Act. 15 U.S.C. 78o(d)(1). An issuer that does not fit within these categories is not required under the federal securities laws to file periodic reports regardless of the volume of off-exchange trading in its shares, even if the issuer has a CUSIP number (as Forum does).

Based on the information in the record, it is unlikely that Forum triggers any of these registration or reporting requirements. Its shares are not listed and do not trade on a registered national securities exchange. Forum shares trade over the counter, and there is nothing to suggest that it has the assets, shareholders of record, or history of having offered and sold securities pursuant to a registration statement that would trigger Section 12(g) registration or a Section 15(d) reporting obligation.[1]

[1] If Forum were required to register or report under Section 12(b), Section 12(g), or Section 15(d), and it failed to register or comply with ongoing reporting requirements, it would be in violation of federal law.

Prior to September 28, 2021, Forum shares traded, if at all, under the symbol FRMB on the "pink sheets"—the common nickname for the "Pink Open Market," which is an interdealer quotation system operated by OTC Markets Group, Inc.. In this "pink tier," ongoing financial reporting to the Commission was not required. And within the pink tier, Forum fit within the "no information" category, which meant Forum had not provided any information to any regulator or to OTC Markets within the prior six months. After September 28, 2021, which was the compliance date for amendments to a Commission rule discussed below, OTC Markets no longer permits broker-dealers to publish proprietary quotations for shares issued by Forum on any market tier operated by OTC Markets. Rather, broker-dealers can only publish unsolicited quotations on OTC Markets' Expert Market tier, which are not publicly available. *See* https://www.otcmarkets.com/stock/FRMB/overview. Additionally, OTC Markets has labeled the securities of Forum on this market as "Caveat Emptor," which is a designation employed by OTC Markets to inform investors "that there is a public interest concern associated with the company, which may include a spam campaign, questionable stock promotion, known investigation of fraudulent activity committed by the company or insiders, regulatory suspensions, or disruptive corporate actions." *Id.*

Synergy seeks Berry's appointment to revive Forum under Delaware law so that Synergy may identify private companies that will engage in a "reverse merger" with Forum. Pet. 9. As a general matter, a reverse merger is a transaction or series of transactions in which a privately held corporation merges with and into a publicly traded corporation, "thereby allowing the private corporation to transform into a publicly [] traded corporation without the necessity of making an initial stock offering." *SEC v. M&A West, Inc.*, 538 F.3d 1043, 1046-47 (9th Cir. 2008). In many instances, including this one, the issuer is a shell entity with minimal assets and no actual operations. *See* 17 C.F.R. 240.12b-2 (for issuers of registered securities, defining a "shell company" to mean a registrant that has "[n]o or nominal operations" and either "(i) [n]o or nominal assets; (ii) [a]ssets consisting solely of cash or cash equivalents; or (iii) [a]ssets consisting of any amount of cash and cash equivalents and nominal other assets"). Although reverse merger transactions may also involve the offer and sale of securities, Synergy does not state in its petition that it plans to issue new securities as part of its request for custodianship or its efforts to identify possible reverse merger targets.

DISCUSSION

Delaware courts have expressed concern that granting relief under Delaware law to enable a reverse merger may conflict with or circumvent the federal securities laws. *E.g., Clabault v. Caribbean Select, Inc.*, 805 A.2d 913, 918 (Del. Ch. 2002); *Williams v. Calypso Wireless, Inc.*, 2012 Del Ch. Lexis 34, at *2 n.1 (Del. Ch. Feb. 8, 2012). However, a reverse merger is not *per se* illegal under the federal securities laws. There is no statute or regulation that precludes a privately held corporation from merging with a shell company in order to obtain access to the capital markets and the investing public. And regardless of whether this Court decides to grant the petition, Forum (and Synergy) must follow all federal securities laws and regulations—compliance with Delaware law will not allow Forum or Synergy to circumvent federal law in this context.

Reverse mergers may pose significant risks to investors in part because they differ from other, more traditional methods of capital formation in terms of the quantity and timing of disclosures to the public. Congress established a statutory framework for the offer and sale of securities in the Securities Act of 1933, which ensures the availability of information to purchasers, and it imposed ongoing and periodic reporting obligations in the Exchange Act. Both statutes had the primary objective of substituting "a philosophy of full disclosure for the philosophy of caveat emptor and thus to achieve a high standard of business ethics in the securities industry." *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 186 (1963). For example, issuers pursuing an initial public offering must file a registration statement containing a prospectus with the Commission before any sales can occur. And issuers offering securities pursuant to the Regulation A exemption from registration must comply with several disclosure and investor-protection mandates, such as qualification of an offering circular by the Commission and a qualified purchaser requirement for certain offerings. The costs associated with satisfying these requirements have prompted some issuers to seek other methods of accessing capital markets, such as reverse mergers.

Within the context of reverse mergers, the amount of information available to investors differs depending on the type of shell company involved. In some instances, a private entity seeks to merge with a shell company that has a reporting obligation, has properly filed its periodic and current reports, and may even have its securities listed on a registered national securities exchange. In that context, investors may have access to some historical and current information, including financial statements, about the issuer. But in other instances, the shell company is a non-reporting issuer that is not required to comply with the reporting requirements of the federal securities laws.

Forum is such a company. It is not currently required to file reports with the Commission, and it does not appear to have filed any quarterly or annual reports for at least a decade.[2] Consequently, investors in Forum will not be able to readily obtain publicly available historical or current information about the company, including its financial status, its management, its ownership, or the risks it faces. By contrast, companies with reporting obligations that are involved in reverse mergers must file with the Commission periodic reports that are available to the public, or they will face significant consequences, including possible trading suspensions and revocation of registration.

Moreover, because Forum is a non-reporting company, it would not be required to file a report regarding any reverse merger that it completes in the future (assuming the reverse merger does not involve the offer and sale of securities). Under regulations that the Commission adopted in 2005—partly in response to concerns about the robustness of disclosures in reverse-merger situations—a reporting company must file a Form 8-K that discloses extensive information about the company being acquired following a transaction in

[2] The Commission's EDGAR system does not reflect any filings by Forum for at least the past 10 years. It appears that Forum may have a predecessor-in-interest named Adsero Corp., which filed a notice of termination of registration under the Exchange Act in May 2008. To the extent that Forum triggers the reporting requirements of the Exchange Act in the future, it must once again register its securities pursuant to the Exchange Act.

which a shell company ceases to be a shell as a result of merging with a formerly private operating business. *Use of Form S-8, Form 8-K, and Form 20-F by Shell Companies*, 70 Fed. Reg. 42234 (Jul. 21, 2005). Within four business days after completion of the transaction, the surviving entity (usually the publicly traded issuer) must effectively file the same type of disclosures that would have to be filed when registering a class of securities under Section 12 of the Exchange Act, including audited financial statements. *Id.* at 42239-40. A non-reporting company like Forum, however, would not be required to file such a Form 8-K if it eventually merges with a private entity, and the public thus would not have access to any additional disclosures following an acquisition.

Forum does not trade on a registered national securities exchange (and the record does not reflect a current intent to seek listing on such an exchange). Thus, it would not need to satisfy the more stringent listing requirements imposed by exchanges for shell companies that combine with private companies in reverse mergers. In the wake of Commission enforcement actions and trading suspensions related to reverse mergers, the New York Stock Exchange proposed a rule, which the Commission approved, that imposed more rigorous listing standards for reverse mergers. *Order*, 76 Fed. Reg. 70795 (Nov. 15, 2011). Among other things, the NYSE's rules require a "seasoning-period" of one year prior to listing during which the post-merger publicly traded entity (*i.e.*, the former shell company) would have to produce financial and other information as part of its required filings. *Id.* at 70798-99. In effect, this requirement ensures that a reverse-merger company will have produced at least one year of audited financial statements, along with other material information, prior to listing on the NYSE. *Id*; *see also Order*, 76 Fed. Reg. 70799 (Nov. 15, 2011) (approving a similar rule proposed by Nasdaq that governs listing standards for reverse-merger companies). Forum is not subject to these standards.

A September 2020 regulatory change, which went fully into effect on September 28, 2021, has ramifications for non-reporting issuers like Forum. The amendments to Exchange Act Rule 15c2-11 restrict the ability of broker-dealers to publish quotations for issuers without current and publicly available information, which will impair the existence of an active market for their shares. Rule 15c2-11 requires broker-dealers, which play a gatekeeping role in facilitating access to OTC markets, including the pink sheets, to review issuer information before initiating or resuming quotations for the issuer's securities in a quotation medium. 17 C.F.R. 240.15c2-11(e)(8) (defining "quotation medium" to mean "any 'interdealer quotation system' or any publication or electronic communications network or other device that is used by brokers or dealers to make known to others their interest in transactions in any security, including offers to buy or sell at a stated price or otherwise, or invitations of offers to buy or sell"). The Commission amended the rule to modernize it, ensure that specified information is publicly available, and boost investor protections. *Publication or Submission of Quotations without Specified Information*, 85 Fed. Reg. 68124 (Oct. 27, 2020). Among other changes, the amendments ensure that broker-dealers do not publish quotations for a security when current information about the issuer is not publicly available. *Id.* at 68133-36. The expanded list of information that a broker-dealer must review includes a complete list of insiders and a "current" balance sheet (*i.e.*, one prepared less than sixteen months before the publication of the quotation). *Id.* at 68135. Unless there is such current

and publicly available information about an issuer, broker-dealers cannot publish or submit a quotation in a quotation medium (absent an applicable exception).

The Commission also updated the "piggyback" exception in Rule 15c2-11 for shell companies, which allows a broker-dealer to rely on a quotation from another broker-dealer that initially complied with the information-review requirement for shell companies. *Id.* at 68151-54. Under the amendments, "a broker-dealer may maintain a quoted market for the security of an issuer that the broker-dealer has a reasonable basis under the circumstance for believing is a shell company by relying on the piggyback exception during the 18-month period following the initial publication or submission of a price bid or offer quotation for the security" in an inter-dealer quotation system, "assuming all other requirements for the piggyback exception are met." *Id.* at 68153. The Commission adopted this time period to "help protect retail investors by preventing such companies, which can be used as vehicles for fraud, from maintaining a quoted market indefinitely, while promoting capital formation by preserving for a time-limited period a cost-effective means for companies to maintain a broker-dealer quoted market." *Id.* at 68151; *see also id. at* 68140, 68143 (stating that the Commission's rulemaking regarding the piggyback exception was "informed by studies that show a greater incidence of litigated cases involving pump-and-dump schemes brought against issuers of OTC securities relative to cases brought against issuers of exchange-listed securities," and that the rulemaking reflected the concern that the OTC market "may attract those seeking to engage in fraudulent practices, such as pump-and-dump schemes, due to a lack of publicly available current information about certain issuers").

Reverse mergers can facilitate access to the capital markets, but they can pose a risk of harm to investors, particularly when they involve issuers with fewer disclosure obligations. Especially for retail investors, investments in these types of securities are associated with negative and volatile returns, as well as illiquidity.[3] Moreover, the Commission has recognized "the potential for investor harm" in the wake of "unregistered reverse mergers" because of "the securities of shell companies being used in fraudulent and manipulative schemes, such as pump-and-dump schemes." *Id.* at 68152, 68188. Indeed, studies have shown that a significant percentage of market manipulation cases involve securities trading on the OTC markets, such as the pink sheets.[4] This occurs, in part, because

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[3] White, *OTC Outcomes*, at 16-23 (studying 1.8 million trades in OTC stocks and finding an annualized median return of –60.3%); Ulf Brüggemann et al., *The Twilight Zone: OTC regulatory regimes and market quality*, Working Paper No. 19358, Nat'l Bureau of Econ. Research (2016) (studying sample of over 10,000 OTC stocks from 2001 to 2010 and finding average and median annual returns of –27% and –37%, respectively); Bjorn Eraker and Mark Ready, *Do investors overpay for stocks with lottery-like payoffs? An examination of the returns of OTC Stocks*, 115 J. Fin. Econ. 486 (2015) (studying a sample of approximately 6,800 OTC stocks between 2000 and 2008 and finding an average –24% annual return after accounting for transaction costs).

[4] *Publication or Submission of Quotations*, 85 Fed. Reg. at 68188 & n.662 (citing staff analysis of 4,000 litigation releases from 2003-2012, which found "that the majority of alleged violations involving issuers of OTC securities were primarily classified as reverse mergers of shell companies or as market manipulation"); Aggarwal & Wu, *Stock Market Manipulations*, 79 J. Bus. 1915 (2006) (examining Commission enforcement actions for market manipulation from 1990-2001, and finding that nearly 50% occurred on OTC markets, including the pink sheets); Cumming & Johan, *Listing Standards and Fraud*, 34 Managerial & Decision Econ. 45 (2013) (finding that 70% of pump-and-dump cases from 2005-2011 involved pink sheet securities).

misrepresentations "about a company are more likely to result in stock price and volume movements if investors lack alternative sources of information, such as well-disseminated, time, and credible disclosures." *OTC Outcomes,* at 11 (citing studies).

The Commission's enforcement program has been active in this area, bringing numerous actions involving reverse mergers and securities for which little information is publicly available. In one instance, a group of defendants made false or misleading statements to tout the stock of an issuer that was a party to a reverse merger, including filing a fraudulent financial statement intended to prompt OTC Markets to remove a "caveat emptor" label, all as part of a pump-and-dump scheme. *SEC v. Zenergy Int'l*, 2016 U.S. Dist. Lexis 127630, at *2-10 (N.D. Ill. 2016). In another example, the Commission halted a pump-and-dump scheme before the "dump" by suspending trading in the wake of a reverse merger followed by false or misleading statements designed to rapidly inflate the value of the resulting company's shares. *SEC v. Madsen,* 2018 U.S. Dist. Lexis 178442, at *3 (S.D.N.Y. Oct. 17, 2018).[5]

In addition to these enforcement actions, the Commission has taken multiple steps, and the staff has issued guidance, to shore up protections for investors in this context. The Commission has promulgated rules, including the amendments to Rule 15c2-11 "as a means reasonably designed to prevent fraudulent, deceptive, or manipulative acts or practices," 17 C.F.R. 240.15c2-11(a), that stem, in part, from the lack of current information about non-reporting entities involved in reverse mergers. And the Office of Investor Education and Advocacy issued an investor bulletin that discussed the risks associated with reverse-mergers. *Investor Bulletin: Reverse Mergers*, https://www.sec.gov/investor/alerts/reversemergers.pdf (Jun. 9, 2011). While these actions increase the flow of information to investors, and offer caution about potential harms, there are still significant risks associated with reverse mergers.

To the extent that a revived Forum seeks to offer or sell new securities in the future, or to register a class of securities under the Exchange Act, it must comply with all laws regarding securities offerings and registration. Any offer or sale of securities must be registered pursuant to the Securities Act of 1933 or the offering must fit within an exemption from registration. All offers and sales are subject to the registration and antifraud provisions of the federal securities laws, including the private rights of action provided by Sections 11 and 12 of the Securities Act.

[5] *E.g.*, *SEC v. Sierra Brokerage Servs.*, 712 F.3d 321 (6th Cir. 2013); *SEC v. M&A West*, 538 F.3d 1043 (9th Cir. 2008); *SEC v. Cavanagh*, 445 F.3d 105 (2d Cir. 2006); *SEC v. Weed*, 315 F. Supp.3d 667 (D. Mass. 2018); *SEC v. Jammin' Java Corp.*, 2016 U.S. Dist. Lexis 184773 (C.D. Cal. Jul. 18, 2016); *SEC v. Strebinger*, 114 F. Supp. 3d 1321 (N.D. Ga. 2015); *SEC v. Brandonisio*, 2013 U.S. Dist. Lexis 136647 (D. Nev. Sep. 24, 2013).

Sincerely,

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