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# The Thorny Path to Public Trading for Unlisted Companies

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# I INTRODUCTION

Companies that “go public” through nontraditional means—i.e., without an initial public offering (IPO) listed on a national securities exchange—face significant challenges to initiating the public trading of their common stock. Such challenges include enabling broker-dealers to publish public quotations on their common stock and qualifying for electronic clearance and settlement of trades through the facilities of The Depository Trust Company (DTC).

This white paper is intended to provide practical guidance to these companies and to help them set investor expectations on when public trading can commence. Surprisingly, it can take months to accomplish what seems to be a simple task.

# I PUBLICATION OF QUOTATIONS

Rule 15c2-11 promulgated by the Securities and Exchange Commission (SEC) under the Securities Exchange Act of 1934, as amended (the Exchange Act), makes it unlawful for a broker or a dealer to publish any quotation for a security unless the broker or the dealer has in its records certain documents and information regarding the issuer of the security that are current and publicly available. The rule applies not to the underlying transactions or the ability of an investor to buy or sell a security but rather to the ability to publish a quotation, or an “indication of interest,” to the greater investing public. Quotations submitted on an “unsolicited” basis are still permitted under the amended rule, subject to additional requirements for insiders and affiliates.

Generally speaking, non-exchange-traded companies may become quoted by having a broker-dealer file and clearing a Form 211 with the Financial Industry Regulatory Authority Inc. (FINRA). Since September 2021, companies have been able to also undergo an “Initial Review” by OTC Markets Group (OTC Markets), which then submits the Form 211 to FINRA. Companies subject to the Form 211 process include private companies looking to generate a trading market, non-U.S. companies listed on a foreign stock exchange, public companies that have become public without doing an offering, and companies that have become delinquent in their reporting obligations.

Rule 15c2-11 contains various exceptions that allow public broker-dealer quotes outside the scope of the rule’s disclosure requirements, including one for securities of well-capitalized issuers that meet the following thresholds:

- Average worldwide daily trading volume of \$100,000;

- \$50 million in assets; and
- \$10 million in shareholders’ equity, based on reported trading volume and the issuer’s recent audited financial statements.

Companies with Exchange Act reporting requirements must make timely filings of all reports required to be filed with the SEC for brokers to be able to continue to publish quotations. Rule 15c2-11 permits Exchange Act reporting companies up to 180 additional days to continue to be eligible for public broker-dealer quotes. Accordingly, companies that make their annual or quarterly reports publicly available (via EDGAR) within 180 days of the end of the applicable quarterly or annual reporting period will still be eligible for broker-dealer proprietary quotes. Regulation CF and Regulation A reporting companies are subject to different time frames under Rule 15c2-11.

Under amendments to Rule 15c2-11, which became effective in 2023, brokers and dealers may not publish quotations for a shell company until it becomes an operating company, and a broker-dealer complies with the information review requirement and files a Form 211 with FINRA. The rule defines a shell company as any issuer that has:

- No or nominal operations; and
- Either:
  - No or nominal assets;
  - Assets consisting solely of cash and cash equivalents; or
  - Assets consisting of any amount of cash and cash equivalents and nominal other assets.

As noted above, since September 2021, OTC Markets has had the ability to conduct the initial

review of a company and submit a Form 211 to FINRA on behalf of companies in lieu of a broker-dealer. Generally, OTC Markets will agree to perform the initial review as part of an issuer's application process for approval to be included in the OTCQX or OTCQB markets.

OTC Markets generally states that it will submit the Form 211 only for companies seeking to list on OTCQX and OTCQB, leaving submissions for OTCID listings to be handled by broker-dealers. Furthermore, OTC Markets has not always been transparent about the companies for which it will handle submissions. Key factors influencing that decision typically include the company's financial and operating history, management evaluation, and industry. Therefore, it is crucial to engage with OTC Markets early in the process to discuss your specific situation.

If the issuer does not meet the criteria for the inclusion of its shares on the OTCQX or the OTCQB or does not intend to apply for such inclusion or if OTC Markets determines that it will not conduct the initial review of an issuer, the issuer must contract with a broker-dealer to compile and submit to FINRA the information required by Form 211.

There are very few broker-dealers who are willing to undergo the time and expense of filing and clearing a Form 211 on behalf of the issuer. In part, this is because FINRA prevents broker-dealers from charging issuers for Form 211 submissions.

Therefore, it is often necessary to refer shareholders to the broker-dealer for stock trades to entice it to make the submission.

Generally speaking, the initial review process by OTC Markets is less burdensome and more reasonable than using a broker-dealer to clear a Form 211 through FINRA. This is in part because OTC Markets can rely on information provided by the issuer as part of its application for inclusion. However, we do not believe that there is a significant difference in the time it takes to clear the Form 211 through FINRA. In addition, the issuer will still need to find a market-maker willing to publish quotations once FINRA clearance is secured.

In our experience, the time required to clear a Form 211 through FINRA is highly variable and uncertain. In some cases, we have seen Form 211s cleared in four months; in other cases, it has taken upward of seven months. Because of this lengthy and uncertain process, issuers seeking to have their securities eligible for quotation should engage service providers who understand the process and can advise on what information FINRA will require as part of the process.

Once FINRA clears a Form 211, the requesting broker-dealer or market-maker can publish quotations on the securities. Other broker-dealers can then "piggyback" on the Form 211 clearance and publish their own quotations.

## **I CUSIP NUMBER**

A CUSIP number is a nine-digit alphanumeric code that is used to identify securities, such as stocks, bonds, and other financial instruments. The CUSIP (Committee on Uniform Securities Identification Procedures) system was developed in the 1960s

to uniquely identify securities and facilitate the settlement of trades.

Each CUSIP number is unique to a specific security, and is assigned by the CUSIP Service Bureau, which is operated by the American Bankers Association.

CUSIP numbers are used by banks, brokerages, and other financial institutions to identify and track securities in their systems, and to facilitate the clearing and settlement of trades. CUSIP numbers are typically found on the front of physical securities, and they can also be found in various

databases and other sources of information about securities.

A CUSIP number is required for any security traded on a U.S. exchange or market. International analogs exist for trading in other countries.

## I DTC ELIGIBILITY

Unless an issuer's common stock is DTC eligible, shares cannot be transferred between brokerage accounts electronically. That makes it much harder for investors to buy or sell shares. Consequently, not being DTC eligible makes it even more difficult for issuers to raise capital or to develop a public trading market for their common stock.

Most U.S.-based stock exchanges, including the New York Stock Exchange and the Nasdaq Stock Market, as well as OTC Markets, require companies to be DTC eligible as a condition of listing or quotation. Furthermore, most large U.S. banks and broker-dealers are direct DTC participants or clear through other DTC participants. Many of these banks and brokerages will not accept shares of companies that are not DTC eligible.

Shares of common stock that are DTC eligible are much easier for investors to buy and sell and will be more actively traded than shares that are not DTC eligible. Among the advantages of DTC eligibility are that:

- Shareholders can transfer and deposit shares with brokers more easily;
- Upgrading a company from standard DTC eligibility to be FAST/DWAC<sup>1</sup> eligible allows the electronic deposit and withdrawal of shares,

significantly reducing the time to issue and transfer shares. Many investors require issuers to be FAST/DWAC eligible; and

- FAST/DWAC eligibility eliminates the hassle of issuing and transferring physical certificates and other related expenses.

Obtaining DTC eligibility requires the issuer to file an application with DTC and to provide certain supporting materials. Normally, DTC eligibility is handled in an initial public offering by the lead managing underwriter coordinating with the new-issues department at DTC. However, in situations where an issuer is applying for DTC eligibility without an offering, the process is typically handled by the broker-dealer conducting the Form 211 submission.

In some cases, the issuer's transfer agent may be able to assist an issuer with the DTC eligibility process. Because DTC eligibility is so important and DTC's non-offering process is so opaque, we believe that a transfer agent's ability to assist with this process should be an important aspect of selecting a transfer agent. In our experience, the large transfer agents do not provide this service.

<sup>1</sup> DWAC is the acronym for Deposit/Withdrawal at Custodian, which permits brokers and custodial banks to request the movement of shares to or from the issuer's transfer agent electronically. A DWAC results in the crediting or debiting of shares to or from DTC's book-entry account on the records of the issuer maintained by the transfer agent bypassing DTC's stock processing unit. Through the DTC FAST program, shareholders are able to hold shares in book-entry electronic form with the transfer agent directly. These shares can be transferred via DWAC from the transfer agent to a broker-dealer and vice versa without having to go through DTC. This speeds up processing times and allows shareholders the option to be issued physical or book-entry certificates. An application for FAST/DWAC eligibility has to be made by the transfer agent.

DTC can deny an application DTC eligibility and is not required to explain the reasons for a denial. In our experience, there are several common reasons why DTC might reject an application. These include:

- History of late filings with the SEC;
- History of several name changes or reverse splits in the past few years; and
- Lawyers, accountants, or stock promoters that have a regulatory history.

If an issuer's application for DTC eligibility is rejected, the issuer can apply again in two to three months, during which time it should work with its counsel and other advisors to eliminate matters that may have led to DTC's rejection.

The Direct Registration System (DRS) allows shareholders of public companies to hold their shares directly on the books of the company's transfer agent in book-entry form without issuing physical stock certificates. The DTC DRS facilitates the movement of investor direct registration positions between financial institutions such as broker-dealers and transfer agents. DRS has several significant advantages, including:

- DRS does not require a medallion guarantee or stock power, whereas DWAC does; and
- Having shares held electronically reduces the cost for corporate actions. Share amounts can be adjusted without having to incur the cost of reissuing physical stock certificates.

To be eligible for DRS:

- The shares must be free trading or eligible for restriction removal.
- The broker or its clearing broker must be a DTC participant.
- The issuer must be DRS eligible.
- The broker must have access to the Participant Terminal System /Participant Browser System.

- The transfer agent must be a DTC limited participant and submit the application for DRS.
- Issuers that are traded on Nasdaq and NYSE are required to be approved for DRS before their IPOs or uplistings are completed.

It is important to note that an issuer's common stock is not eligible for clearance through DTC until a shareholder deposits physical shares in exchange for book-entry securities. Because restricted shares are not eligible for clearance through DTC, an issuer must have at least one shareholder who is legally entitled to hold unlegended shares, either because the shares have been registered, they are freely tradeable without restriction under Rule 144 of the Securities Act, or they have been held for so long that counsel is able to opine that the shares do not require a restrictive legend. In certain cases, it can be difficult to find a shareholder who holds shares meeting these requirements who is able to assist the issuer in making the initial deposit. As a result, issuers should consider the need to meet this requirement sooner rather than later in the process.

# **I CONCLUSION**

For companies navigating an alternative path to becoming public, the process of commencing the public trading of their common stock can be an arcane, bewildering, and frustrating process. It is important for these issuers to be as informed about the process as possible and to engage a transfer agent and counsel that assist them in navigating the process. Good advisors will be able to reduce the frustration involved in the process and may be able to save their clients time and money in the pursuit of a public trading market.

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Specializing in corporate finance and mergers and acquisitions, [Jack Hogoboom](#) has represented buyers, sellers, issuers, underwriters and investors in hundreds of transactions over his more than 35 years of practice. He has represented public and private clients in all types of transactions including IPOs, public and private domestic and cross-border offerings, and public and private acquisitions in a wide range of industries including business services, consumer products, technology, life sciences, chemical, renewables, media, and natural resources. Jack has been listed in both the securities law and corporate law categories in *The Best Lawyers in America* since 2007. Often quoted in legal publications, he frequently publishes articles and speaks on corporate finance issues.

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Dan Carter is a seasoned leader with extensive experience in finance and technology, where he emphasizes value creation within collaborative and growth-oriented contexts. His areas of expertise include initial public offerings (IPOs) and exchange listings; compliance, structuring, and introductions related to equity raises; Blue Sky compliance and multi-jurisdictional filings across all 50 states; and the preparation and submission of EDGAR and iXBRL filings for SEC registrants.



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Jason Carter is a financial executive with broad expertise spanning corporate formation, consulting, and financing across multiple sectors, including technology, healthcare, biotechnology, medical devices, and mining. He has extensive experience guiding companies through the transition from private to public markets, drawing on a background that includes roles as a transfer agent, market maker, and broker, as well as participation in investment banking transactions totaling more than \$37 million. His areas of specialization include investor relations, equity financing, capital structure, financial analysis, business development, market making, regulatory compliance (including Rule 15c2-11, DTC eligibility, and securities filings), and both EDGAR and XBRL reporting. Jason has also served as an expert witness in cases involving securities valuation and trading mechanics.

# I ABOUT

## Lowenstein Sandler LLP

Lowenstein Sandler LLP is a national law firm with over 375 lawyers based in New York, Palo Alto, New Jersey, Utah, and Washington, D.C. The firm represents leaders in virtually every sector of the global economy, with particular emphasis on investment funds, life sciences, and technology. Recognized for its entrepreneurial spirit and high standard of client service, the firm is committed to the interests of its clients, colleagues, and communities.

## Colonial Stock Transfer Company, Inc.

Colonial Stock Transfer Company, Inc. is a stock transfer agent headquartered in the historical stock exchange district in Salt Lake City. Colonial provides stock transfer agent and issuer compliance services to public companies listed on the NYSE, NASDAQ and OTC Markets and offers a full suite of services for privately-held companies. Established in 1987, Colonial provides issuers and shareholders the most professional, cost effective and innovative services in the industry by going beyond standard transfer agency agendas and incorporating a more personal touch with competent, efficient employees and unmatched customer service.