MoFo Classics: Rule 144A and Regulation S Offerings

April 2, 2015, 8:30AM – 9:45AM EST

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Rule 144A and Regulation S: The Rules and Current Practices

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Rule 144A
Rule 144A – A Brief Overview

- Rule 144A under the Securities Act of 1933 (the “Securities Act”), provides a (non-exclusive) safe harbor from Section 5’s registration requirements for resales of restricted securities to “qualified institutional buyers” (“QIBs”).
- The premise: not all investors need the full protections of the prospectus requirements of the Securities Act.
- The rule applies to offers made by persons other than the issuer of the securities – resales.
- The rule applies to securities that are not listed on a U.S. national securities exchange or quoted on a U.S. automated inter-dealer quotation system.
  - So, no such thing as a Rule 144A offering of an issuer’s listed common stock.
Rule 144A – Overview (cont’d)

- A reseller may rely on any available exemption from the registration requirements of the Securities Act when selling restricted securities (e.g., Rule 144 under the Securities Act (“Rule 144”) or Regulation S under the Securities Act).

- Securities acquired in Rule 144A transactions are deemed to be “restricted securities” under Rule 144.
Rule 144A – The Basic Offering Structure

- The issuer initially sells restricted securities to investment bank(s) in a Securities Act Section 4(a)(2) or Regulation D private placement.
- The investment bank immediately resells the securities to QIBs under Rule 144A under the Securities Act (“Rule 144A”).

Issuer → Initial Purchaser → QIBs

- Often combined with a Regulation S offering.
Rule 144A – Principal Documentation

- Offering Memorandum
  - May contain similar information to a full Form S-1 or F-1 prospectus, or may be much shorter.
  - May incorporate by reference the issuer’s filings with the SEC, or a non-U.S. regulator.
  - For significant offerings, the scope of disclosure tends to be comparable to a public offering, as the underwriters are concerned about potential liabilities, and expect “10b-5” representations from the issuer, and legal opinions from counsel.
  - Due diligence by counsel will generally be similar to that performed in a public offering.

- A purchase agreement between the issuer and the underwriter(s)
  - Similar to an underwriting agreement in terms of representations, covenants, closing conditions and indemnities.

- Legal opinions
- Comfort letters
- In the case of an A/B exchange offer (“Exxon Capital”), a registration rights agreement.
Rule 144A – How are these offerings conducted?

• In some ways, similar to a registered offering.
• “Road show” with a preliminary offering memorandum, addressed to institutional investors.
• Confirmation of orders with the final offering memorandum (the offering memorandum may be delivered electronically).
• The purchase agreement is executed at pricing, together with the delivery of a comfort letter.
• Closing on a “T+3” basis, or as otherwise agreed with the investors.
• Publicity: generally limited to a Rule 135(c) compliant press release, although general solicitation is now permitted.
Rule 144A – MTN Programs

• In addition to individual offerings, an issuer may have a “Rule 144A program” for multiple offerings.
• Used for repeat offerings, often by financial institution and insurance company issuers, to institutional investors.
• Often used for structured products sold to QIBs.
• Advantages over a public MTN program:
  • No need to publicly disclose innovative structures or sensitive information such as underwriter compensation, investor’s strategies.
  • Limit FINRA filing and other compliance requirements.
  • For financial institution issuers, greater flexibility as to timing of programs when the stock of an underlying security is on a “watch list.”
  • No SEC filing fees.
  • In principle, lower liability profile, and reduced possibility of regulatory review.
Rule 144A – Exxon Capital Exchange Offers

- Methodology is based principally on a 1988 no-action letter and subsequent SEC guidance.
- Securities are privately placed under Rule 144A, and then promptly exchanged for substantially identical securities that have been registered under the Securities Act (either on Form S-4 or F-4).
- Goal: combines the benefits of (a) Rule 144A (quick offering without SEC review) and (b) offering registered securities (liquidity for investors).
- Issuer typically pays “penalty interest” if registration is not effective within a specified period of time.
- Alternative to Exxon Capital: register the Rule 144A securities for resale on Form S-3 or F-3.
  - Problem: identifying selling shareholders in a prospectus.
  - Problem: resale registration statement will require continued effectiveness of a shelf registration.
Integration and Exxon Capital Exchange Offers

• Registration Statement is filed – can more securities be issued?
• Reopening before effectiveness of the Form S-4:
  • Institutional investors not solicited by registration statement.
  • Issue new securities, and increase amount registered in exchange offering.
• Reopening after effectiveness of the Form S-4/After Completion of the Exchange Offer:
  • Need new Rule 144A offering (or shelf offering). These new Rule 144A securities will not be fungible with the ones registered in the exchange offering.
  • New exchange offer in the case of a “follow-on” Rule 144A offering.
Rule 144A – Conditions for an Offering

- Resales only to a QIB, or to a purchaser that the reseller or any persons acting on its behalf reasonably believe to be a QIB.
- The QIB must purchase for its own account or for the account of another QIB.
- Reseller must take steps to ensure that the buyer is aware that the reseller may rely on Rule 144A in connection with such resale.
- The securities resold (a) when issued were not of the “same class” as securities listed on a U.S. national securities exchange or quoted on a U.S. automated inter-dealer quotation system and (b) are not securities of an open-end investment company,UIT, etc.
- For an issuer that is not a reporting company or exempt from reporting pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934, as amended, the holder and a prospective buyer designated by the holder must have the right to obtain from the issuer, upon the holder’s request, certain reasonably current information.
Rule 144A – What is a QIB?

• The following qualify as “QIBs”:
  • Any corporation, partnership or other entity (but not an individual) that owns and invests on a consolidated basis $100 million in the aggregate in securities of non-affiliates (other than bank deposits and loan participations, repurchase agreements and securities subject thereto, and currency, interest rate and commodity swaps);
  • Registered dealers that own or invest $10 million of such non-affiliate securities or are engaged in “riskless principal transactions” on behalf of QIBs (to qualify, the QIB must commit to the broker-dealer that the QIB will simultaneously purchase the securities from the broker-dealer);
  • Any investment company that is part of a “family” that has the same investment adviser and together own $100 million of such non-affiliate securities; and
  • Any U.S. or foreign bank or S&L that owns and invests on a consolidated basis $100 million in such non-affiliate securities and has a net worth of at least $25 million.

• A QIB can be formed solely for purpose of conducting a Rule 144A transaction.

• In determining whether a purchaser qualifies as a QIB, a seller can rely on published financial statements or a certificate of an executive officer of the issuer.
Rule 144A – How can a reseller ascertain that a purchaser is a QIB?

- A reseller may rely on the following (as long as the information is no more than 16 months old):
  - the purchaser’s most recent publicly available annual financial statements;
  - information filed with the SEC or another government agency or self-regulatory organization;
  - information in a recognized securities manual, such as Moody’s or S&P;
  - certification by the purchaser’s chief financial or other executive officer specifying the amount of securities owned and invested as of the end of the purchaser’s most recent fiscal year; and
  - a QIB questionnaire.

- The SEC acknowledges that the reseller may use other information to establish a reasonable belief of eligibility.
Rule 144A – Legending

• The reseller will make the buyer aware that the security is a Rule 144A security by:
  • legending the security (i.e., the security must include language that it is not registered under the Securities Act);
  • including an appropriate statement in the offering memorandum;
  • obtaining an agreement that the purchaser understands that the securities must be resold pursuant to an exemption or registration under the Securities Act; and
  • by obtaining a restricted CUSIP number.

• A recurring issue in offerings of Canadian securities that have a public listing.
Rule 144A – “Same Class” Determination

- How does one determine whether the securities are of the “same class” as those listed or quoted on an exchange?
  - Common stock
    - If it is of substantially similar character and the holders enjoy substantially similar rights.
    - Note: if ADR’s are publicly traded in the U.S., the underlying securities would also be considered publicly traded.
  - Preferred stock
    - If its terms relating to dividends, liquidation preference, voting rights, convertibility, redemption and similar characteristics are substantially identical.
  - Convertible or exchangeable security
    - If it has an effective conversion premium on issuance (at pricing) of less than 10% and a warrant with a term less than three years or an effective exercise premium on issuance (at pricing) of less than 10%, will be treated as the “same class” as the underlying security.
    - SEC Release No. 33-6862 (1990) provide examples of how to calculate the effective conversion premium.
Rule 144A – Current Information Requirements

- For securities of a non-public company, the holder and a prospective purchaser designated by the holder have the right to obtain from the issuer, upon request, the following information:
  - a brief statement of the nature of the business of the issuer and its products and services; and
  - the issuer's most recent balance sheet and profit and loss and retained earnings statements, and similar financial statements for such part of the two preceding fiscal years as the issuer has been in operation.
- The financial statements should be audited, to the extent reasonably available.
- The information must be reasonably current.
Rule 144A – Time of Sale Information

- Although Rule 159 is not expressly applicable to Rule 144A offerings, many investment banks apply the same treatment, in order to help reduce the risk of liability.
- Use of term sheets and offering memoranda supplements, to ensure that all material information is conveyed to investors at the time of pricing.
- Counsel is typically expected to opine as to the “disclosure package,” as in the case of a public offering.
Regulation S
Regulation S – Overview

• Regulation S under the Securities Act ("Reg S") provides an exemption from the registration requirements of Section 5 of the Securities Act for securities offered and sold outside the U.S. to non-U.S. persons.

• The premise: "principles of comity." (To be clear, not "comedy.")

• Recurring themes: whether the securities are to be purchased outside of the U.S., and the risk of flowback into the U.S.

• Reg S (Rules 901 to 905 under the Securities Act) provides non-exclusive safe harbors for (1) offers and sales by issuers, distributors and their affiliates and (2) resales by others (i.e., investors).

• In practice, issuers try to comply with the safe harbors, particularly in connection with a significant primary offering. However, if an issuer fails to comply with a specific safe harbor, it may still argue that the registration requirements should not apply to the transaction.
Regulation S – Overview (cont’d)

• In general: (1) there must be an “offshore transaction” (i.e., an offer cannot be made to a person in the U.S. (“U.S. person”) and the buyer must be outside the U.S. or the seller must reasonably believe the buyer is outside the U.S.) and (2) neither the issuer nor any distributor (or any affiliate of either) may engage in any “directed selling efforts” (i.e., activities that may condition the U.S. market for the securities).

• For many offerings:
  • there is a “distribution compliance period” during which no offer or sale may be made to a U.S. person for 40 days or, in some cases, for one year; and
  • the offering documents and underwriting agreements must reflect certain restrictions on sales to U.S. persons.
Regulation S – Rule 903 – Sales by an Issuer

- Most “Regulation S offerings” are Rule 903 offerings.
- Rule 903 provides an issuer safe harbor for sales of securities offshore.
  - Directed selling efforts made by the issuer or any distributor will eliminate the safe harbor.
    - Result: robust representations and covenants.
    - Prohibition applies during the distribution, and any “distribution compliance period.”
- Three categories of securities, based on the probability of flowback into the U.S. and the type/amount of information available in the U.S., the first category being the least restrictive, and the third is the most restrictive.
  - Different restrictions apply to equity and debt securities. For purposes of the categories, warrants are treated like equity securities and convertible securities are treated like the underlying security.
Categories 1, 2 and 3

• Criteria:
  • Nationality of the issuer.
  • Reporting status of the issuer under the 1934 Act.
  • Degree of U.S. market interest in the issuer’s securities.

• Implications of the Criteria:
  • Foreign issuers are generally subject to fewer restrictions.
  • Offerings by reporting issuers would require fewer restrictions because of the availability of information.
  • Securities with U.S. market interest would generally be subject to more restrictions.
Regulation S – Category 1 (Easiest)

- Securities must be sold in an “offshore transaction” – as defined in Rule 902.
- Category 1 includes:
  - Securities of foreign issuers with no “substantial U.S. market interest” (see below) in the equity or debt securities to be offered, or in the case of warrants or convertible securities, the underlying securities.
  - Securities sold in an “overseas directed offering” (discussed below) by U.S. or non-U.S. issuers.
  - Foreign government securities.
  - Securities sold under eligible employee benefit plans.
- Additional transactional restrictions: None.
- “Overseas directed offering” means an offering directed to residents of a single foreign country in accordance with local laws, limited to straight debt, asset-backed securities or non-participating preferred stock denominated in a foreign currency and not convertible into U.S. dollar denominated securities.
Regulation S – Category 2

• Things get more complicated.
• Category 2 includes the following securities:
  • Debt securities of issuers that are reporting companies or non-reporting foreign issuers.
  • Equity securities of foreign issuers that are reporting companies.
  • Convertible debt of foreign issuers that are reporting companies.
• Additional transactional restrictions:
  • No offer or sale to U.S. persons may be made during a 40-day distribution compliance period commencing on the closing date or the date the securities were first offered to persons not engaged in the distribution (note: the issuer must devise a means to ensure compliance).
  • Distributors of the securities must advise certain securities professionals to whom they sell of the restricted period.
  • Offers and sales by a distributor of an unsold allotment or subscription are deemed to be made during the restricted period, regardless of when the offers and sales are actually made. However, once a distributor sells an allotment after the restricted period to a non-U.S. person, the security may be resold immediately.
Regulation S – Category 3

• Things get noticeably more complicated.
• Category 3 includes securities of any type that are not covered by Categories 1 and 2.
• Additional transactional restrictions:
  • All Category 2 restrictions are applicable.
  • Equity securities:
    • Distribution compliance period is one year.
    • If the offer or sale is made prior to the expiration of the distribution compliance period then:
      • purchasers must certify that they are not U.S. persons or purchasing for the account of U.S. persons,
      • purchasers must agree that any resale will be made pursuant to Reg S, registration under the Securities Act or an applicable exemption and not to engage in hedging transactions unless in compliance with the Securities Act,
      • domestic issuers must legend the securities,
      • the issuer is required by contract or by its charter, bylaws or similar document not to register any transfer made in violation of Reg S and
      • each distributor selling securities to a distributor, dealer or person receiving a selling fee or other remuneration prior to the end of the distribution compliance period must notify the purchaser that the purchaser is subject to the same restrictions on offers and sales as the distributor.
  • Debt securities:
    • Distribution compliance period is 40 days.
    • During the distribution compliance period, the debt securities must be represented by a temporary global certificate.
    • Definitive securities may only be issued after the end of the distribution compliance period, and only upon certification of ownership by a non-U.S. person or a U.S. person that acquired the security in a transaction not requiring registration.
In order to qualify for both safe harbors, the offer or sale must be made in an “offshore transaction.”

- No offer is made to a person in the U.S.
- Either of the following additional conditions must be met:
  - At the time of the buy order, the buyer is, or the seller reasonably believed that the buyer is, outside the U.S., or
  - The transaction is executed on (1) a physical trading floor of an established foreign securities exchange, in the case of Rule 903, or (2) on a designated offshore securities market and the seller does not know that the transaction has been pre-arranged with a buyer in the U.S., in the case of Rule 904.
Regulation S – Directed Selling Efforts

• In order to qualify for both safe harbors, no “directed selling efforts” may be made in the U.S.
• Directed selling efforts include the following:
  • Mailing printed materials to U.S. investors.
  • Conducting promotional seminars in the U.S.
  • Placing advertisements in a publication with a general circulation in the U.S.
  • Placing advertisements with radio or television stations broadcast in the U.S.
  • Making offers directed at identifiable groups of U.S. citizens in a foreign country (e.g., members of the U.S. military).
Regulation S – Directed Selling Efforts (cont’d)

• Permitted activities include the following:
  • Advertisements required to be published under foreign law.
  • Communications with persons excluded from the definition of U.S. person.
  • Tombstone advertisements in publications with less than 20% of their circulation in the U.S.
  • Bona fide visits to real estate facilities by prospective investors.
  • Quotations of a foreign broker-dealer distributed by a third-party system that primarily distributes such information in foreign countries, provided that no security transaction can be executed through the system between broker-dealers and persons in the U.S. and contact with U.S. persons is not initiated.
  • Proper notice under Securities Act Rule 135 that an issuer intends to make a registered public offering of its securities.
  • Providing journalists with access to issuer meetings held outside the U.S., or providing written press or press-related materials released outside the U.S. in compliance with Securities Act Rule 135.
  • Isolated limited contact.
  • Routine advertising unrelated to selling efforts.
  • Customary and legal activities conducted outside of the U.S.
Regulation S – Directed Selling Efforts (cont’d)

• For Reg S offerings with a Rule 144A tranche, the SEC has clarified that general solicitation and general advertising in connection with a Rule 144A offering will not be viewed as “directed selling efforts” in connection with a concurrent Reg S offering.
  • This is particularly relevant because general solicitation and general advertising are now permitted for Rule 144A offerings (so long as the securities are sold to a QIB or to a purchaser that the seller and any person acting on the seller’s behalf reasonably believes is a QIB).
  • As a result, issuers are now permitted to broadly disseminate a press release regarding a proposed or completed Rule 144A offering free of the prior restrictions on the types of permitted information under Securities Act Rule 135c.
Regulation S – Substantial U.S. Market Interest

• “Substantial U.S. market interest” means:
  • Equity: In the shorter of the last fiscal year or since the issuer incorporated: (a) the single largest market for such class of securities was in the U.S. or (b) 20% of trading took place in the U.S. and less than 55% of such trading took place in a single foreign market.
  • Debt: (a) $1 billion or more of debt securities are held by U.S. persons, (b) 20% or more of the issuer’s debt securities are held by U.S. persons and (c) the issuer’s debt securities are held of record by 300 or more U.S. persons.
  • Warrants and convertible securities: For warrants, the level of market interest in the underlying securities, and for convertible securities, the level of market interest in either the convertible security or the security into which it may be converted.
The following are “U.S. persons”: 

- Any natural person in the U.S.
- Any partnership or corporation organized or incorporated under the laws of the U.S.
- Any estate of which any executor or administrator is a U.S. person.
- Any trust of which any trustee is a U.S. person.
- Any agency or branch of a foreign entity located in the U.S.
- Any non-discretionary account or similar account (other than an estate or trust) held by a dealer or other fiduciary organized, incorporated or (if an individual) residing in the U.S.
- Any partnership or corporation, if: 
  - Organized or incorporated under the laws of any foreign jurisdiction; and
  - Formed by a U.S. person principally for the purpose of investing in securities not registered under the Securities Act, unless it is organized or incorporated, and owned, by accredited investors (as defined in Rule 501(a) under Regulation D) who are not natural persons, estates or trusts.
Regulation S – Rule 904

• Rule 904 provides a safe harbor for resales of securities offshore.
  • Resales by (a) any persons other than the issuer and (b) any officer or director of the issuer or who is an affiliate solely by virtue of holding such position, are deemed to have occurred outside the U.S., if the general conditions of Reg S apply (i.e., the offering is offshore and there are no directed selling efforts) and any applicable additional resale requirements are met.

• Additional resale requirements
  • Resales by dealers and persons receiving selling concessions: May resell the securities in Categories 2 and 3 during the applicable restricted period only if they reasonably believe the offeree or buyer is not a U.S. person; and if the seller or its representative knows that the purchaser is a dealer, or is a person receiving a selling concession or other fee as to the securities, the seller or its representative must notify the buyer of the applicable distribution compliance period.
  • Resales by certain affiliates: For an offer or sale by an officer or director of the issuer, who is an affiliate of the issuer or distributor by holding that position, no selling concession, fee or other remuneration is paid in connection with the offer or sale other than the usual and customary broker’s commission that would be received by a person executing the transaction as an agent.
Regulation S – Rule 905

• Rule 905 imposes resale limitations for equity securities.
  • Equity securities acquired from the issuer, a distributor or their respective affiliates in a transaction subject to the conditions of Rules 901 or 903 are deemed to be restricted securities as defined in Rule 144.
  • An offshore purchaser therefore can resell such securities only in accordance with Reg S or the registration requirements of the Securities Act.
  • Any restricted securities or equity securities of a domestic issuer will continue to be restricted securities despite the fact that such securities were acquired in a resale transaction pursuant to Rule 904.
  • The resale of restricted securities offshore under the safe harbor does not eliminate the restricted status of such securities.
Regulation S Offering Documents

• Can vary considerably, depending upon the jurisdictions in which sales are made, and degree of regulation in the relevant jurisdictions.
• Size of offering, relevant types of investors, types of legal opinions contemplated will all dictate the scope of the disclosure.
• And of course, Regulation S contemplates appropriate language and legends for Category 2 and Category 3 offerings.
§230.144A Private resales of securities to institutions.

Preliminary Notes: 1. This section relates solely to the application of section 5 of the Act and not to antifraud or other provisions of the federal securities laws.

2. Attempted compliance with this section does not act as an exclusive election; any seller hereunder may also claim the availability of any other applicable exemption from the registration requirements of the Act.

3. In view of the objective of this section and the policies underlying the Act, this section is not available with respect to any transaction or series of transactions that, although in technical compliance with this section, is part of a plan or scheme to evade the registration provisions of the Act. In such cases, registration under the Act is required.

4. Nothing in this section obviates the need for any issuer or any other person to comply with the securities registration or broker-dealer registration requirements of the Securities Exchange Act of 1934 (the Exchange Act), whenever such requirements are applicable.

5. Nothing in this section obviates the need for any person to comply with any applicable state law relating to the offer or sale of securities.

6. Securities acquired in a transaction made pursuant to the provisions of this section are deemed to be restricted securities within the meaning of §230.144(a)(3) of this chapter.

7. The fact that purchasers of securities from the issuer thereof may purchase such securities with a view to reselling such securities pursuant to this section will not affect the availability to such issuer of an exemption under section 4(a)(2) of the Act, or Regulation D under the Act, from the registration requirements of the Act.

(a) Definitions. (1) For purposes of this section, qualified institutional buyer shall mean:

(i) Any of the following entities, acting for its own account or the accounts of other qualified institutional buyers, that in the aggregate owns and invests on a discretionary basis at least $100 million in securities of issuers that are not affiliated with the entity:

(A) Any insurance company as defined in section 2(a)(13) of the Act;

NOTE: A purchase by an insurance company for one or more of its separate accounts, as defined by section 2(a)(37) of the Investment Company Act of 1940 (the “Investment Company Act”), which are neither registered under section 8 of the Investment Company Act nor required to be so registered, shall be deemed to be a purchase for the account of such insurance company.

(B) Any investment company registered under the Investment Company Act or any business
development company as defined in section 2(a)(48) of that Act;

(C) Any Small Business Investment Company licensed by the U.S. Small Business Administration under section 301(c) or (d) of the Small Business Investment Act of 1958;

(D) Any plan established and maintained by a state, its political subdivisions, or any agency or instrumentality of a state or its political subdivisions, for the benefit of its employees;

(E) Any employee benefit plan within the meaning of title I of the Employee Retirement Income Security Act of 1974;

(F) Any trust fund whose trustee is a bank or trust company and whose participants are exclusively plans of the types identified in paragraph (a)(1)(i) (D) or (E) of this section, except trust funds that include as participants individual retirement accounts or H.R. 10 plans.

(G) Any business development company as defined in section 202(a)(22) of the Investment Advisers Act of 1940;

(H) Any organization described in section 501(c)(3) of the Internal Revenue Code, corporation (other than a bank as defined in section 3(a)(2) of the Act or a savings and loan association or other institution referenced in section 3(a)(5)(A) of the Act or a foreign bank or savings and loan association or equivalent institution), partnership, or Massachusetts or similar business trust; and

(I) Any investment adviser registered under the Investment Advisers Act.

(ii) Any dealer registered pursuant to section 15 of the Exchange Act, acting for its own account or the accounts of other qualified institutional buyers, that in the aggregate owns and invests on a discretionary basis at least $10 million of securities of issuers that are not affiliated with the dealer, Provided. That securities constituting the whole or a part of an unsold allotment to or subscription by a dealer as a participant in a public offering shall not be deemed to be owned by such dealer;

(iii) Any dealer registered pursuant to section 15 of the Exchange Act acting in a riskless principal transaction on behalf of a qualified institutional buyer;

NOTE: A registered dealer may act as agent, on a non-discretionary basis, in a transaction with a qualified institutional buyer without itself having to be a qualified institutional buyer.

(iv) Any investment company registered under the Investment Company Act, acting for its own account or for the accounts of other qualified institutional buyers, that is part of a family of investment companies which own in the aggregate at least $100 million in securities of issuers, other than issuers that are affiliated with the investment company or are part of such family of investment companies. Family of investment companies means any two or more investment companies registered under the Investment Company Act, except for a unit investment trust whose assets consist solely of shares of one or more registered investment companies, that have the same investment adviser (or, in the case of unit investment trusts, the same depositor), Provided That, for purposes of this section:

(A) Each series of a series company (as defined in Rule 18f-2 under the Investment Company Act [17 CFR 270.18f-2]) shall be deemed to be a separate investment company; and

(B) Investment companies shall be deemed to have the same adviser (or depositor) if their advisers (or depositors) are majority-owned subsidiaries of the same parent, or if one investment company's adviser (or depositor) is a majority-owned subsidiary of the other investment company's adviser (or depositor);

(v) Any entity, all of the equity owners of which are qualified institutional buyers, acting for its own account or the accounts of other qualified institutional buyers; and

(vi) Any bank as defined in section 3(a)(2) of the Act, any savings and loan association or other institution as referenced in section 3(a)(5)(A) of the Act, or any foreign bank or savings and loan association or equivalent institution, acting for its own account or the accounts of other qualified
institutional buyers, that in the aggregate owns and invests on a discretionary basis at least $100 million in securities of issuers that are not affiliated with it and that has an audited net worth of at least $25 million as demonstrated in its latest annual financial statements, as of a date not more than 16 months preceding the date of sale under the Rule in the case of a U.S. bank or savings and loan association, and not more than 18 months preceding such date of sale for a foreign bank or savings and loan association or equivalent institution.

(2) In determining the aggregate amount of securities owned and invested on a discretionary basis by an entity, the following instruments and interests shall be excluded: bank deposit notes and certificates of deposit; loan participations; repurchase agreements; securities owned but subject to a repurchase agreement; and currency, interest rate and commodity swaps.

(3) The aggregate value of securities owned and invested on a discretionary basis by an entity shall be the cost of such securities, except where the entity reports its securities holdings in its financial statements on the basis of their market value, and no current information with respect to the cost of those securities has been published. In the latter event, the securities may be valued at market for purposes of this section.

(4) In determining the aggregate amount of securities owned by an entity and invested on a discretionary basis, securities owned by subsidiaries of the entity that are consolidated with the entity in its financial statements prepared in accordance with generally accepted accounting principles may be included if the investments of such subsidiaries are managed under the direction of the entity, except that, unless the entity is a reporting company under section 13 or 15(d) of the Exchange Act, securities owned by such subsidiaries may not be included if the entity itself is a majority-owned subsidiary that would be included in the consolidated financial statements of another enterprise.

(5) For purposes of this section, riskless principal transaction means a transaction in which a dealer buys a security from any person and makes a simultaneous offsetting sale of such security to a qualified institutional buyer, including another dealer acting as riskless principal for a qualified institutional buyer.

(6) For purposes of this section, effective conversion premium means the amount, expressed as a percentage of the security's conversion value, by which the price at issuance of a convertible security exceeds its conversion value.

(7) For purposes of this section, effective exercise premium means the amount, expressed as a percentage of the warrant's exercise value, by which the sum of the price at issuance and the exercise price of a warrant exceeds its exercise value.

(b) Sales by persons other than issuers or dealers. Any person, other than the issuer or a dealer, who offers or sells securities in compliance with the conditions set forth in paragraph (d) of this section shall be deemed not to be engaged in a distribution of such securities and therefore not to be an underwriter of such securities within the meaning of sections 2(a)(11) and 4(a)(1) of the Act.

(c) Sales by dealers. Any dealer who offers or sells securities in compliance with the conditions set forth in paragraph (d) of this section shall be deemed not to be a participant in a distribution of such securities within the meaning of section 4(a)(3)(C) of the Act and not to be an underwriter of such securities within the meaning of section 2(a)(11) of the Act, and such securities shall be deemed not to have been offered to the public within the meaning of section 4(a)(3)(A) of the Act.

(d) Conditions to be met. To qualify for exemption under this section, an offer or sale must meet the following conditions:

(1) The securities are sold only to a qualified institutional buyer or to a purchaser that the seller and any person acting on behalf of the seller reasonably believe is a qualified institutional buyer. In determining whether a prospective purchaser is a qualified institutional buyer, the seller and any person acting on its behalf shall be entitled to rely upon the following non-exclusive methods of establishing the prospective purchaser's ownership and discretionary investments of securities:

(i) The prospective purchaser's most recent publicly available financial statements, Provided That such statements present the information as of a date within 16 months preceding the date of sale of
securities under this section in the case of a U.S. purchaser and within 18 months preceding such date of sale for a foreign purchaser;

(ii) The most recent publicly available information appearing in documents filed by the prospective purchaser with the Commission or another United States federal, state, or local governmental agency or self-regulatory organization, or with a foreign governmental agency or self-regulatory organization, Provided That any such information is as of a date within 16 months preceding the date of sale of securities under this section in the case of a U.S. purchaser and within 18 months preceding such date of sale for a foreign purchaser;

(iii) The most recent publicly available information appearing in a recognized securities manual, Provided That such information is as of a date within 16 months preceding the date of sale of securities under this section in the case of a U.S. purchaser and within 18 months preceding such date of sale for a foreign purchaser; or

(iv) A certification by the chief financial officer, a person fulfilling an equivalent function, or other executive officer of the purchaser, specifying the amount of securities owned and invested on a discretionary basis by the purchaser as of a specific date on or since the close of the purchaser’s most recent fiscal year, or, in the case of a purchaser that is a member of a family of investment companies, a certification by an executive officer of the investment adviser specifying the amount of securities owned by the family of investment companies as of a specific date on or since the close of the purchaser’s most recent fiscal year;

(2) The seller and any person acting on its behalf takes reasonable steps to ensure that the purchaser is aware that the seller may rely on the exemption from the provisions of section 5 of the Act provided by this section;

(3) The securities offered or sold:

(i) Were not, when issued, of the same class as securities listed on a national securities exchange registered under section 6 of the Exchange Act or quoted in a U.S. automated inter-dealer quotation system; Provided, That securities that are convertible or exchangeable into securities so listed or quoted at the time of issuance and that had an effective conversion premium of less than 10 percent, shall be treated as securities of the class into which they are convertible or exchangeable; and that warrants that may be exercised for securities so listed or quoted at the time of issuance, for a period of less than 3 years from the date of issuance, or that had an effective exercise premium of less than 10 percent, shall be treated as securities of the class to be issued upon exercise; and Provided further, That the Commission may from time to time, taking into account then-existing market practices, designate additional securities and classes of securities that will not be deemed of the same class as securities listed on a national securities exchange or quoted in a U.S. automated inter-dealer quotation system; and

(ii) Are not securities of an open-end investment company, unit investment trust or face-amount certificate company that is or is required to be registered under section 8 of the Investment Company Act; and

(4)(i) In the case of securities of an issuer that is neither subject to section 13 or 15(d) of the Exchange Act, nor exempt from reporting pursuant to Rule 12g3-2(b) (§240.12g3-2(b) of this chapter) under the Exchange Act, nor a foreign government as defined in Rule 405 (§230.405 of this chapter) eligible to register securities under Schedule B of the Act, the holder and a prospective purchaser designated by the holder have the right to obtain from the issuer, upon request of the holder, and the prospective purchaser has received from the issuer, the seller, or a person acting on either of their behalf, at or prior to the time of sale, upon such prospective purchaser's request to the holder or the issuer, the following information (which shall be reasonably current in relation to the date of resale under this section): a very brief statement of the nature of the business of the issuer and the products and services it offers; and the issuer's most recent balance sheet and profit and loss and retained earnings statements, and similar financial statements for such part of the two preceding fiscal years as the issuer has been in operation (the financial statements should be audited to the extent reasonably available).

(ii) The requirement that the information be reasonably current will be presumed to be satisfied if:
(A) The balance sheet is as of a date less than 16 months before the date of resale, the statements of profit and loss and retained earnings are for the 12 months preceding the date of such balance sheet, and if such balance sheet is not as of a date less than 6 months before the date of resale, it shall be accompanied by additional statements of profit and loss and retained earnings for the period from the date of such balance sheet to a date less than 6 months before the date of resale; and

(B) The statement of the nature of the issuer's business and its products and services offered is as of a date within 12 months prior to the date of resale; or

(C) With regard to foreign private issuers, the required information meets the timing requirements of the issuer's home country or principal trading markets.

(e) Offers and sales of securities pursuant to this section shall be deemed not to affect the availability of any exemption or safe harbor relating to any previous or subsequent offer or sale of such securities by the issuer or any prior or subsequent holder thereof.

§230.901 General statement.

For the purposes only of section 5 of the Act (15 U.S.C. §77e), the terms offer, offer to sell, sell, sale, and offer to buy shall be deemed to include offers and sales that occur within the United States and shall be deemed not to include offers and sales that occur outside the United States.
Title 17: Commodity and Securities Exchanges
PART 230—GENERAL RULES AND REGULATIONS, SECURITIES ACT OF 1933

§230.902 Definitions.

As used in Regulation S, the following terms shall have the meanings indicated.

(a) Debt securities. “Debt securities” of an issuer is defined to mean any security other than an equity security as defined in §230.405, as well as the following:

(1) Non-participatory preferred stock, which is defined as non-convertible capital stock, the holders of which are entitled to a preference in payment of dividends and in distribution of assets on liquidation, dissolution, or winding up of the issuer, but are not entitled to participate in residual earnings or assets of the issuer; and

(2) Asset-backed securities, which are securities of a type that either:

(i) Represent an ownership interest in a pool of discrete assets, or certificates of interest or participation in such assets (including any rights designed to assure servicing, or the receipt or timeliness of receipt by holders of such assets, or certificates of interest or participation in such assets, of amounts payable thereunder), provided that the assets are not generated or originated between the issuer of the security and its affiliates; or

(ii) Are secured by one or more assets or certificates of interest or participation in such assets, and the securities, by their terms, provide for payments of principal and interest (if any) in relation to payments or reasonable projections of payments on assets meeting the requirements of paragraph (a) (2)(i) of this section, or certificates of interest or participations in assets meeting such requirements.

(iii) For purposes of paragraph (a)(2) of this section, the term “assets” means securities, installment sales, accounts receivable, notes, leases or other contracts, or other assets that by their terms convert into cash over a finite period of time.

(b) Designated offshore securities market. “Designated offshore securities market” means:

(1) The Eurobond market, as regulated by the International Securities Market Association; the Alberta Stock Exchange; the Amsterdam Stock Exchange; the Australian Stock Exchange Limited; the Bermuda Stock Exchange; the Bourse de Bruxelles; the Copenhagen Stock Exchange; the European Association of Securities Dealers Automated Quotation; the Frankfurt Stock Exchange; the Helsinki Stock Exchange; The Stock Exchange of Hong Kong Limited; the Irish Stock Exchange; the Istanbul Stock Exchange; the Johannesburg Stock Exchange; the London Stock Exchange; the Bourse de Luxembourg; the Mexico Stock Exchange; the Borsa Valori di Milan; the Montreal Stock Exchange; the Oslo Stock Exchange; the Bourse de Paris; the Stock Exchange of Singapore Ltd.; the Stockholm Stock Exchange; the Tokyo Stock Exchange; the Toronto Stock Exchange; the Vancouver Stock Exchange; the Warsaw Stock Exchange and the Zurich Stock Exchange; and

(2) Any foreign securities exchange or non-exchange market designated by the Commission.
Attributes to be considered in determining whether to designate an offshore securities market, among others, include:

(i) Organization under foreign law;
(ii) Association with a generally recognized community of brokers, dealers, banks, or other professional intermediaries with an established operating history;
(iii) Oversight by a governmental or self-regulatory body;
(iv) Oversight standards set by an existing body of law;
(v) Reporting of securities transactions on a regular basis to a governmental or self-regulatory body;
(vi) A system for exchange of price quotations through common communications media; and
(vii) An organized clearance and settlement system.

(c) Directed selling efforts. (1) “Directed selling efforts” means any activity undertaken for the purpose of, or that could reasonably be expected to have the effect of, conditioning the market in the United States for any of the securities being offered in reliance on this Regulation S (§230.901 through §230.905, and Preliminary Notes). Such activity includes placing an advertisement in a publication “with a general circulation in the United States” that refers to the offering of securities being made in reliance upon this Regulation S.

(2) Publication “with a general circulation in the United States”:

(i) Is defined as any publication that is printed primarily for distribution in the United States, or has had, during the preceding twelve months, an average circulation in the United States of 15,000 or more copies per issue; and

(ii) Will encompass only the U.S. edition of any publication printing a separate U.S. edition if the publication, without considering its U.S. edition, would not constitute a publication with a general circulation in the United States.

(3) The following are not “directed selling efforts”:

(i) Placing an advertisement required to be published under U.S. or foreign law, or under rules or regulations of a U.S. or foreign regulatory or self-regulatory authority, provided the advertisement contains no more information than legally required and includes a statement to the effect that the securities have not been registered under the Act and may not be offered or sold in the United States (or to a U.S. person, if the advertisement relates to an offering under Category 2 or 3 (paragraph (b)(2) or (b)(3)) in §230.903) absent registration or an applicable exemption from the registration requirements;

(ii) Contact with persons excluded from the definition of “U.S. person” pursuant to paragraph (k)(2)(vi) of this section or persons holding accounts excluded from the definition of “U.S. person” pursuant to paragraph (k)(2)(i) of this section, solely in their capacities as holders of such accounts;

(iii) A tombstone advertisement in any publication with a general circulation in the United States, provided:

(A) The publication has less than 20% of its circulation, calculated by aggregating the circulation of its U.S. and comparable non-U.S. editions, in the United States;

(B) Such advertisement contains a legend to the effect that the securities have not been registered under the Act and may not be offered or sold in the United States (or to a U.S. person, if the advertisement relates to an offering under Category 2 or 3 (paragraph (b)(2) or (b)(3)) in §230.903) absent registration or an applicable exemption from the registration requirements; and

(C) Such advertisement contains no more information than:
(1) The issuer's name;
(2) The amount and title of the securities being sold;
(3) A brief indication of the issuer's general type of business;
(4) The price of the securities;
(5) The yield of the securities, if debt securities with a fixed (non-contingent) interest provision;
(6) The name and address of the person placing the advertisement, and whether such person is participating in the distribution;
(7) The names of the managing underwriters;
(8) The dates, if any, upon which the sales commenced and concluded;
(9) Whether the securities are offered or were offered by rights issued to security holders and, if so, the class of securities that are entitled or were entitled to subscribe, the subscription ratio, the record date, the dates (if any) upon which the rights were issued and expired, and the subscription price; and
(10) Any legend required by law or any foreign or U.S. regulatory or self-regulatory authority;

(iv) Bona fide visits to real estate, plants or other facilities located in the United States and tours thereof conducted for a prospective investor by an issuer, a distributor, any of their respective affiliates or a person acting on behalf of any of the foregoing;

(v) Distribution in the United States of a foreign broker-dealer's quotations by a third-party system that distributes such quotations primarily in foreign countries if:

(A) Securities transactions cannot be executed between foreign broker-dealers and persons in the United States through the system; and
(B) The issuer, distributors, their respective affiliates, persons acting on behalf of any of the foregoing, foreign broker-dealers and other participants in the system do not initiate contacts with U.S. persons or persons within the United States, beyond those contacts exempted under §240.15a-6 of this chapter;

(vi) Publication by an issuer of a notice in accordance with §230.135 or §230.135c;

(vii) Providing any journalist with access to press conferences held outside of the United States, to meetings with the issuer or selling security holder representatives conducted outside the United States, or to written press-related materials released outside the United States, at or in which a present or proposed offering of securities is discussed, if the requirements of §230.135e are satisfied; and

(viii) Publication or distribution of a research report by a broker or dealer in accordance with Rule 138(c) (§230.138(c)) or Rule 139(b) (§230.139(b)).

(d) **Distributor.** “Distributor” means any underwriter, dealer, or other person who participates, pursuant to a contractual arrangement, in the distribution of the securities offered or sold in reliance on this Regulation S (§230.901 through §230.905, and Preliminary Notes).

(e) **Domestic issuer/Foreign issuer.** “Domestic issuer” means any issuer other than a “foreign government” or “foreign private issuer” (both as defined in §230.405). “Foreign issuer” means any issuer other than a “domestic issuer.”

(f) **Distribution compliance period.** “Distribution compliance period” means a period that begins when the securities were first offered to persons other than distributors in reliance upon this Regulation S (§230.901 through §230.905, and Preliminary Notes) or the date of closing of the offering, whichever is later, and continues until the end of the period of time specified in the relevant provision of §230.903, except that:
(1) All offers and sales by a distributor of an unsold allotment or subscription shall be deemed to be made during the distribution compliance period;

(2) In a continuous offering, the distribution compliance period shall commence upon completion of the distribution, as determined and certified by the managing underwriter or person performing similar functions;

(3) In a continuous offering of non-convertible debt securities offered and sold in identifiable tranches, the distribution compliance period for securities in a tranche shall commence upon completion of the distribution of such tranche, as determined and certified by the managing underwriter or person performing similar functions; and

(4) That in a continuous offering of securities to be acquired upon the exercise of warrants, the distribution compliance period shall commence upon completion of the distribution of the warrants, as determined and certified by the managing underwriter or person performing similar functions, if requirements of §230.903(b)(5) are satisfied.

(g) Offering restrictions. “Offering restrictions” means:

(1) Each distributor agrees in writing:

(i) That all offers and sales of the securities prior to the expiration of the distribution compliance period specified in Category 2 or 3 (paragraph (b)(2) or (b)(3)) in §230.903, as applicable, shall be made only in accordance with the provisions of §230.903 or §230.904; pursuant to registration of the securities under the Act; or pursuant to an available exemption from the registration requirements of the Act; and

(ii) For offers and sales of equity securities of domestic issuers, not to engage in hedging transactions with regard to such securities prior to the expiration of the distribution compliance period specified in Category 2 or 3 (paragraph (b)(2) or (b)(3)) in §230.903, as applicable, unless in compliance with the Act; and

(2) All offering materials and documents (other than press releases) used in connection with offers and sales of the securities prior to the expiration of the distribution compliance period specified in Category 2 or 3 (paragraph (b)(2) or (b)(3)) in §230.903, as applicable, shall include statements to the effect that the securities have not been registered under the Act and may not be offered or sold in the United States or to U.S. persons (other than distributors) unless the securities are registered under the Act, or an exemption from the registration requirements of the Act is available. For offers and sales of equity securities of domestic issuers, such offering materials and documents also must state that hedging transactions involving those securities may not be conducted unless in compliance with the Act. Such statements shall appear:

(i) On the cover or inside cover page of any prospectus or offering circular used in connection with the offer or sale of the securities;

(ii) In the underwriting section of any prospectus or offering circular used in connection with the offer or sale of the securities; and

(iii) In any advertisement made or issued by the issuer, any distributor, any of their respective affiliates, or any person acting on behalf of any of the foregoing. Such statements may appear in summary form on prospectus cover pages and in advertisements.

(h) Offshore transaction. (1) An offer or sale of securities is made in an “offshore transaction” if:

(i) The offer is not made to a person in the United States; and

(ii) Either:

(A) At the time the buy order is originated, the buyer is outside the United States, or the seller and any person acting on its behalf reasonably believe that the buyer is outside the United States; or
(B) For purposes of:

(1) Section 230.903, the transaction is executed in, on or through a physical trading floor of an established foreign securities exchange that is located outside the United States; or

(2) Section 230.904, the transaction is executed in, on or through the facilities of a designated offshore securities market described in paragraph (b) of this section, and neither the seller nor any person acting on its behalf knows that the transaction has been pre-arranged with a buyer in the United States.

(2) Notwithstanding paragraph (h)(1) of this section, offers and sales of securities specifically targeted at identifiable groups of U.S. citizens abroad, such as members of the U.S. armed forces serving overseas, shall not be deemed to be made in “offshore transactions.”

(3) Notwithstanding paragraph (h)(1) of this section, offers and sales of securities to persons excluded from the definition of “U.S. person” pursuant to paragraph (k)(2)(vi) of this section or persons holding accounts excluded from the definition of “U.S. person” pursuant to paragraph (k)(2)(i) of this section, solely in their capacities as holders of such accounts, shall be deemed to be made in “offshore transactions.”

(4) Notwithstanding paragraph (h)(1) of this section, publication or distribution of a research report in accordance with Rule 138(c) (§230.138(c)) or Rule 139(b) (§230.139(b)) by a broker or dealer at or around the time of an offering in reliance on Regulation S (§§230.901 through 230.905) will not cause the transaction to fail to be an offshore transaction as defined in this section.

(i) Reporting issuer. “Reporting issuer” means an issuer other than an investment company registered or required to register under the 1940 Act that:

(1) Has a class of securities registered pursuant to Section 12(b) or 12(g) of the Exchange Act (15 U.S.C. 78l(b) or 78l(g)) or is required to file reports pursuant to Section 15(d) of the Exchange Act (15 U.S.C. 78o(d)); and

(2) Has filed all the material required to be filed pursuant to Section 13(a) or 15(d) of the Exchange Act (15 U.S.C. 78m(a) or 78o(d)) for a period of at least twelve months immediately preceding the offer or sale of securities made in reliance upon this Regulation S (§§230.901 through 230.905, and Preliminary Notes) (or for such shorter period that the issuer was required to file such material).

(j) Substantial U.S. market interest. (1) “Substantial U.S. market interest” with respect to a class of an issuer’s equity securities means:

(i) The securities exchanges and inter-dealer quotation systems in the United States in the aggregate constituted the single largest market for such class of securities in the shorter of the issuer’s prior fiscal year or the period since the issuer’s incorporation; or

(ii) 20 percent or more of all trading in such class of securities took place in, on or through the facilities of securities exchanges and inter-dealer quotation systems in the United States and less than 55 percent of such trading took place in, on or through the facilities of securities markets of a single foreign country in the shorter of the issuer’s prior fiscal year or the period since the issuer’s incorporation.

(2) “Substantial U.S. market interest” with respect to an issuer’s debt securities means:

(i) Its debt securities, in the aggregate, are held of record (as that term is defined in §240.12g5-1 of this chapter and used for purposes of paragraph (j)(2) of this section) by 300 or more U.S. persons;

(ii) $1 billion or more of: The principal amount outstanding of its debt securities, the greater of liquidation preference or par value of its securities described in §230.902(a)(1), and the principal amount or principal balance of its securities described in §230.902(a)(2), in the aggregate, is held of record by U.S. persons; and

(iii) 20 percent or more of: The principal amount outstanding of its debt securities, the greater of
liquidation preference or par value of its securities described in §230.902(a)(1), and the principal amount
or principal balance of its securities described in §230.902(a)(2), in the aggregate, is held of record by
U.S. persons.

(3) Notwithstanding paragraph (j)(2) of this section, substantial U.S. market interest with respect to
an issuer's debt securities is calculated without reference to securities that qualify for the exemption
provided by Section 3(a)(3) of the Act (15 U.S.C. 77c(a)(3)).

(k) U.S. person. (1) “U.S. person” means:

(i) Any natural person resident in the United States;

(ii) Any partnership or corporation organized or incorporated under the laws of the United States;

(iii) Any estate of which any executor or administrator is a U.S. person;

(iv) Any trust of which any trustee is a U.S. person;

(v) Any agency or branch of a foreign entity located in the United States;

(vi) Any non-discretionary account or similar account (other than an estate or trust) held by a dealer
or other fiduciary for the benefit or account of a U.S. person;

(vii) Any discretionary account or similar account (other than an estate or trust) held by a dealer or
other fiduciary organized, incorporated, or (if an individual) resident in the United States; and

(viii) Any partnership or corporation if:

(A) Organized or incorporated under the laws of any foreign jurisdiction; and

(B) Formed by a U.S. person principally for the purpose of investing in securities not registered
under the Act, unless it is organized or incorporated, and owned, by accredited investors (as defined in
§230.501(a)) who are not natural persons, estates or trusts.

(2) The following are not “U.S. persons”:

(i) Any discretionary account or similar account (other than an estate or trust) held for the benefit or
account of a non-U.S. person by a dealer or other professional fiduciary organized, incorporated, or (if
an individual) resident in the United States;

(ii) Any estate of which any professional fiduciary acting as executor or administrator is a U.S.
person if:

(A) An executor or administrator of the estate who is not a U.S. person has sole or shared
investment discretion with respect to the assets of the estate; and

(B) The estate is governed by foreign law;

(iii) Any trust of which any professional fiduciary acting as trustee is a U.S. person, if a trustee who
is not a U.S. person has sole or shared investment discretion with respect to the trust assets, and no
beneficiary of the trust (and no settlor if the trust is revocable) is a U.S. person;

(iv) An employee benefit plan established and administered in accordance with the law of a country
other than the United States and customary practices and documentation of such country;

(v) Any agency or branch of a U.S. person located outside the United States if:

(A) The agency or branch operates for valid business reasons; and

(B) The agency or branch is engaged in the business of insurance or banking and is subject to
substantive insurance or banking regulation, respectively, in the jurisdiction where located; and
(vi) The International Monetary Fund, the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the United Nations, and their agencies, affiliates and pension plans, and any other similar international organizations, their agencies, affiliates and pension plans.


§230.903 Offers or sales of securities by the issuer, a distributor, any of their respective affiliates, or any person acting on behalf of any of the foregoing; conditions relating to specific securities.

(a) An offer or sale of securities by the issuer, a distributor, any of their respective affiliates, or any person acting on behalf of any of the foregoing, shall be deemed to occur outside the United States within the meaning of §230.901 if:

(1) The offer or sale is made in an offshore transaction;

(2) No directed selling efforts are made in the United States by the issuer, a distributor, any of their respective affiliates, or any person acting on behalf of any of the foregoing; and

(3) The conditions of paragraph (b) of this section, as applicable, are satisfied.

(b) Additional conditions—(1) Category 1. No conditions other than those set forth in §230.903(a) apply to securities in this category. Securities are eligible for this category if:

(i) The securities are issued by a foreign issuer that reasonably believes at the commencement of the offering that:

(A) There is no substantial U.S. market interest in the class of securities to be offered or sold (if equity securities are offered or sold);

(B) There is no substantial U.S. market interest in its debt securities (if debt securities are offered or sold);

(C) There is no substantial U.S. market interest in the securities to be purchased upon exercise (if warrants are offered or sold); and

(D) There is no substantial U.S. market interest in either the convertible securities or the underlying securities (if convertible securities are offered or sold);

(ii) The securities are offered and sold in an overseas directed offering, which means:

(A) An offering of securities of a foreign issuer that is directed into a single country other than the United States to the residents thereof and that is made in accordance with the local laws and customary practices and documentation of such country; or

(B) An offering of non-convertible debt securities of a domestic issuer that is directed into a single country other than the United States to the residents thereof and that is made in accordance with the local laws and customary practices and documentation of such country, provided that the principal and interest of the securities (or par value, as applicable) are denominated in a currency other than U.S.
dollars and such securities are neither convertible into U.S. dollar-denominated securities nor linked to U.S. dollars (other than through related currency or interest rate swap transactions that are commercial in nature) in a manner that in effect converts the securities to U.S. dollar-denominated securities.

(iii) The securities are backed by the full faith and credit of a foreign government; or

(iv) The securities are offered and sold to employees of the issuer or its affiliates pursuant to an employee benefit plan established and administered in accordance with the law of a country other than the United States, and customary practices and documentation of such country, provided that:

(A) The securities are issued in compensatory circumstances for bona fide services rendered to the issuer or its affiliates in connection with their businesses and such services are not rendered in connection with the offer or sale of securities in a capital-raising transaction;

(B) Any interests in the plan are not transferable other than by will or the laws of descent or distribution;

(C) The issuer takes reasonable steps to preclude the offer and sale of interests in the plan or securities under the plan to U.S. residents other than employees on temporary assignment in the United States; and

(D) Documentation used in connection with any offer pursuant to the plan contains a statement that the securities have not been registered under the Act and may not be offered or sold in the United States unless registered or an exemption from registration is available.

(2) Category 2. The following conditions apply to securities that are not eligible for Category 1 (paragraph (b)(1)) of this section and that are equity securities of a reporting foreign issuer, or debt securities of a reporting issuer or of a non-reporting foreign issuer.

(i) Offering restrictions are implemented;

(ii) The offer or sale, if made prior to the expiration of a 40-day distribution compliance period, is not made to a U.S. person or for the account or benefit of a U.S. person (other than a distributor); and

(iii) Each distributor selling securities to a distributor, a dealer, as defined in section 2(a)(12) of the Act (15 U.S.C. 77b(a)(12)), or a person receiving a selling concession, fee or other remuneration in respect of the securities sold, prior to the expiration of a 40-day distribution compliance period, sends a confirmation or other notice to the purchaser stating that the purchaser is subject to the same restrictions on offers and sales that apply to a distributor.

(3) Category 3. The following conditions apply to securities that are not eligible for Category 1 or 2 (paragraph (b)(1) or (b)(2)) of this section:

(i) Offering restrictions are implemented;

(ii) In the case of debt securities:

(A) The offer or sale, if made prior to the expiration of a 40-day distribution compliance period, is not made to a U.S. person or for the account or benefit of a U.S. person (other than a distributor); and

(B) The securities are represented upon issuance by a temporary global security which is not exchangeable for definitive securities until the expiration of the 40-day distribution compliance period and, for persons other than distributors, until certification of beneficial ownership of the securities by a non-U.S. person or a U.S. person who purchased securities in a transaction that did not require registration under the Act;

(iii) In the case of equity securities:

(A) The offer or sale, if made prior to the expiration of a one-year distribution compliance period (or six-month distribution compliance period if the issuer is a reporting issuer), is not made to a U.S. person
or for the account or benefit of a U.S. person (other than a distributor); and

(B) The offer or sale, if made prior to the expiration of a one-year distribution compliance period (or six-month distribution compliance period if the issuer is a reporting issuer), is made pursuant to the following conditions:

(1) The purchaser of the securities (other than a distributor) certifies that it is not a U.S. person and is not acquiring the securities for the account or benefit of any U.S. person or is a U.S. person who purchased securities in a transaction that did not require registration under the Act;

(2) The purchaser of the securities agrees to resell such securities only in accordance with the provisions of this Regulation S (§§230.901 through 230.905, and Preliminary Notes), pursuant to registration under the Act, or pursuant to an available exemption from registration; and agrees not to engage in hedging transactions with regard to such securities unless in compliance with the Act;

(3) The securities of a domestic issuer contain a legend to the effect that transfer is prohibited except in accordance with the provisions of this Regulation S (§§230.901 through 230.905, and Preliminary Notes), pursuant to registration under the Act, or pursuant to an available exemption from registration; and that hedging transactions involving those securities may not be conducted unless in compliance with the Act;

(4) The issuer is required, either by contract or a provision in its bylaws, articles, charter or comparable document, to refuse to register any transfer of the securities not made in accordance with the provisions of this Regulation S (§§230.901 through 230.905, and Preliminary Notes), pursuant to registration under the Act, or pursuant to an available exemption from registration; provided, however, that if the securities are in bearer form or foreign law prevents the issuer of the securities from refusing to register securities transfers, other reasonable procedures (such as a legend described in paragraph (b)(3)(iii)(B)(3) of this section) are implemented to prevent any transfer of the securities not made in accordance with the provisions of this Regulation S; and

(iv) Each distributor selling securities to a distributor, a dealer (as defined in section 2(a)(12) of the Act (15 U.S.C. 77b(a)(12)), or a person receiving a selling concession, fee or other remuneration, prior to the expiration of a 40-day distribution compliance period in the case of debt securities, or a one-year distribution compliance period (or six-month distribution compliance period if the issuer is a reporting issuer) in the case of equity securities, sends a confirmation or other notice to the purchaser stating that the purchaser is subject to the same restrictions on offers and sales that apply to a distributor.

(4) **Guaranteed securities.** Notwithstanding paragraphs (b)(1) through (b)(3) of this section, in offerings of debt securities fully and unconditionally guaranteed as to principal and interest by the parent of the issuer of the debt securities, only the requirements of paragraph (b) of this section that are applicable to the offer and sale of the guarantee must be satisfied with respect to the offer and sale of the guaranteed debt securities.

(5) **Warrants.** An offer or sale of warrants under Category 2 or 3 (paragraph (b)(2) or (b)(3)) of this section also must comply with the following requirements:

(i) Each warrant must bear a legend stating that the warrant and the securities to be issued upon its exercise have not been registered under the Act and that the warrant may not be exercised by or on behalf of any U.S. person unless registered under the Act or an exemption from such registration is available;

(ii) Each person exercising a warrant is required to give:

(A) Written certification that it is not a U.S. person and the warrant is not being exercised on behalf of a U.S. person; or

(B) A written opinion of counsel to the effect that the warrant and the securities delivered upon exercise thereof have been registered under the Act or are exempt from registration thereunder; and

(iii) Procedures are implemented to ensure that the warrant may not be exercised within the United
States, and that the securities may not be delivered within the United States upon exercise, other than in offerings deemed to meet the definition of “offshore transaction” pursuant to §230.902(h), unless registered under the Act or an exemption from such registration is available.

ELECTRONIC CODE OF FEDERAL REGULATIONS

e-CFR Data is current as of March 30, 2015

Title 17 → Chapter II → Part 230 → §230.904

Title 17: Commodity and Securities Exchanges
PART 230—GENERAL RULES AND REGULATIONS, SECURITIES ACT OF 1933

§230.904 Offshore resales.

(a) An offer or sale of securities by any person other than the issuer, a distributor, any of their respective affiliates (except any officer or director who is an affiliate solely by virtue of holding such position), or any person acting on behalf of any of the foregoing, shall be deemed to occur outside the United States within the meaning of §230.901 if:

(1) The offer or sale are made in an offshore transaction;

(2) No directed selling efforts are made in the United States by the seller, an affiliate, or any person acting on their behalf; and

(3) The conditions of paragraph (b) of this section, if applicable, are satisfied.

(b) Additional conditions—(1) Resales by dealers and persons receiving selling concessions. In the case of an offer or sale of securities prior to the expiration of the distribution compliance period specified in Category 2 or 3 (paragraph (b)(2) or (b)(3)) of §230.903, as applicable, by a dealer, as defined in Section 2(a)(12) of the Act (15 U.S.C. 77b(a)(12)), or a person receiving a selling concession, fee or other remuneration in respect of the securities offered or sold:

(i) Neither the seller nor any person acting on its behalf knows that the offeree or buyer of the securities is a U.S. person; and

(ii) If the seller or any person acting on the seller's behalf knows that the purchaser is a dealer, as defined in Section 2(a)(12) of the Act (15 U.S.C. 77b(a)(12)), or is a person receiving a selling concession, fee or other remuneration in respect of the securities sold, the seller or a person acting on the seller's behalf sends to the purchaser a confirmation or other notice stating that the securities may be offered and sold during the distribution compliance period only in accordance with the provisions of this Regulation S (§230.901 through §230.905, and Preliminary Notes); pursuant to registration of the securities under the Act; or pursuant to an available exemption from the registration requirements of the Act.

(2) Resales by certain affiliates. In the case of an offer or sale of securities by an officer or director of the issuer or a distributor, who is an affiliate of the issuer or distributor solely by virtue of holding such position, no selling concession, fee or other remuneration is paid in connection with such offer or sale other than the usual and customary broker's commission that would be received by a person executing such transaction as agent.

[63 FR 9646, Feb. 25, 1998]
§230.905 Resale limitations.

Equity securities of domestic issuers acquired from the issuer, a distributor, or any of their respective affiliates in a transaction subject to the conditions of §230.901 or §230.903 are deemed to be “restricted securities” as defined in §230.144. Resales of any of such restricted securities by the offshore purchaser must be made in accordance with this Regulation S (§230.901 through §230.905, and Preliminary Notes), the registration requirements of the Act or an exemption therefrom. Any “restricted securities,” as defined in §230.144, that are equity securities of a domestic issuer will continue to be deemed to be restricted securities, notwithstanding that they were acquired in a resale transaction made pursuant to §230.901 or §230.904.

[63 FR 9647, Feb. 25, 1998]
FREQUENTLY ASKED QUESTIONS ABOUT RULE 144A

Understanding Rule 144A

What is Rule 144A?

Rule 144A is a safe harbor exemption from the registration requirements of Section 5 of the Securities Act for certain offers and sales of qualifying securities by certain persons other than the issuer of the securities. The exemption applies to resales of securities to qualified institutional buyers, who are commonly referred to as “QIBs.” QIBs must be institutions, and cannot be individuals—no matter how wealthy or sophisticated. See “What is a ‘QIB’?”

The securities eligible for resale under Rule 144A are securities of U.S. and foreign issuers that are not listed on a U.S. securities exchange or quoted on a U.S. automated inter-dealer quotation system. See “What is the definition of a U.S. national securities exchange or automated inter-dealer quotation system for purposes of Rule 144A?”

Rule 144A provides that reoffers and resales in compliance with the rule are not “distributions” and that the reseller is therefore not an “underwriter” within the meaning of Section 2(a)(11) of the Securities Act. A reseller that is not the issuer, an underwriter, or a dealer can rely on the exemption provided by Section 4(a)(1) of the Securities Act. Resellers that are dealers can rely on the exemption provided by Section 4(a)(3) of the Securities Act. See “Who may rely on Rule 144A?”

Who may rely on Rule 144A?

Any person other than an issuer may rely on Rule 144A. Issuers must find another exemption for the offer and sale of unregistered securities. Typically they rely on Section 4(a)(2) (often in reliance on Regulation D) or Regulation S under the Securities Act. Affiliates of the issuer may rely on Rule 144A.


What types of transactions are conducted under Rule 144A?

The following types of transactions often are conducted under Rule 144A:

- offerings of debt or preferred securities by public companies;
- offerings by foreign issuers that do not want to become subject to U.S. reporting requirements; and

An issuer that intends to engage in multiple offerings may have a “Rule 144A program.” Rule 144A programs are programs established for offering securities (usually debt securities) on an ongoing or continuous basis to potential offerees. They are similar to “medium-term note programs,” but they are unregistered, and the securities are sold only to QIBs. These programs often are used by financial institution and insurance company issuers to offer securities, through one or more broker-dealers, to institutional investors in continuous offerings. Among the advantages of using Rule 144A programs are (1) no required public disclosure of innovative structures or sensitive information; (2) limited FINRA filing requirements; and (3) reduced potential for liability under the Securities Act.

What are the conditions that a reseller of restricted securities must satisfy to rely on Rule 144A?

There are four conditions to reliance on Rule 144A:

• The resale is made only to QIBs (see “What is a ‘QIB?’” below) or to a purchaser that the reseller (and any person acting on its behalf) reasonably believes is a QIB (see “How does a reseller establish a reasonable belief that a person is a QIB?”);

• The reseller (or any person acting on its behalf) must take reasonable steps to ensure that the buyer is aware that the reseller may rely on Rule 144A in connection with the resale (see “Reseller’s Reasonable Steps So Buyer is Aware of Rule 144A Reliance” below);

• The securities reoffered or resold (a) when issued were not of the same class as securities listed on a U.S. national securities exchange (which includes the NASDAQ Market System) or quoted on a U.S. automated inter-dealer quotation system); and (b) are not securities of an open-end investment company, unit investment trust, or face-amount certificate company that is, or is required to be, registered under the Investment Company Act of 1940; and

• In the case of securities of an issuer that is neither an Exchange Act reporting company, or a foreign issuer exempt from reporting pursuant to Rule 12g3-2(b) of the Exchange Act, or a foreign government, the holder and a prospective buyer designated by the holder must have the right to obtain from the issuer and must receive, upon request, certain “reasonably current” information about the issuer. See “Informational Requirements”.

Source: Rule 144A(d).

Must a reseller of restricted securities rely only on Rule 144A in making exempt resales?

No; Rule 144A is a non-exclusive safe harbor. A reseller may rely upon any applicable exemption from the registration requirements of the Securities Act in connection with the resale of restricted securities.

In addition, Rule 144A offerings often are effected side-by-side with an offering targeted at foreign holders
in reliance on Regulation S. This permits an issuer to effect a multinational offering with a QIB tranche and a Regulation S tranche, and to sell to an initial purchaser outside the United States in reliance on Regulation S, even though the initial purchaser contemplates the immediate resale to QIBs in reliance on Rule 144A.

Typically, resellers that cannot rely on the safe harbor under Rule 144A will attempt to rely on the hybrid Section 4(a)(1½) exemption. See “What is the Section 4(a)(1½) exemption?” In addition, the holder of securities purchased under Rule 144A may rely on the provisions of Rule 144 to sell those securities.

Are securities resold under Rule 144A freely tradable after such resale?

No. Securities acquired in a Rule 144A transaction are deemed to be “restricted securities” within the meaning of Rule 144(a)(3) of the Securities Act. As a result, these securities remain restricted until the applicable holding period expires and may only be publicly resold under Rule 144, pursuant to an effective registration statement, or in reliance on any other available exemption under the Securities Act. Exempt resales of restricted securities may be made in compliance with Rule 144A, the so-called Section 4(a)(1½) exemption, or Regulation S. See “What is the Rule 4(a)(1½) exemption?”

Source: Preliminary Note No. 6 of Rule 144A.

What are the holding periods applicable to the sale of Rule 144A and other restricted securities?

In December 2007, the SEC amended Rule 144, effective February 2008, to, among other things, shorten the holding periods for restricted securities (subject to certain public information requirements).

For non-affiliate holders of restricted securities, Rule 144 provides a safe harbor for the resale of such securities without limitation after six months in the case of issuers that are reporting companies that comply with the current information requirements of Rule 144(c), and after one year in the case of non-reporting issuers. (Prior to the December 2007 amendments, the holding period was one year.) In each case, after a one-year holding period, resales of these securities by non-affiliates will no longer be subject to any other conditions under Rule 144.

For a reporting issuer, compliance with the adequate current public information condition requires the issuer to have filed all required reports under Section 13 or Section 15(d) of the Exchange Act. For a non-reporting issuer, compliance with the adequate current public information condition requires the public availability of basic information about the issuer, including certain financial statements.

For affiliate holders of restricted securities, Rule 144 provides a safe harbor permitting resales of restricted securities, subject to the same six-month and one-year holding periods for non-affiliates and to other resale conditions of amended Rule 144. These other resale conditions include, to the extent applicable: (a) adequate current public information about the issuer, (b) volume limitations, (c) manner of sale requirements for equity securities, and (d) notice filings on Form 144.

Due to the shortened holding periods, it has become easier for Rule 144A securities to be acquired by non-QIBs once the restricted period has expired. Accordingly, the December 2007 amendments decrease the incremental value that registration rights previously provided. See “Why do Rule 144A purchasers typically
insist that the issuer register the securities issued in the Rule 144A transaction?”


What is the Section 4(a)(1½) exemption?
The Section 4(a)(1½) exemption is a case law-derived exemption that allows the resale of privately placed securities in a subsequent private placement.

The Section 4(a)(1½) exemption is designed to permit sellers of securities to rely on Section 4(a)(1) (which provides an exemption for non-issuers, underwriters, and dealers) to avoid underwriter status by implementing the same kinds of restrictions that would be required in the case of a Section 4(a)(2) offering by the issuer itself.

The Section 4(a)(1½) exemption typically is relied on in connection with the resale of restricted securities to accredited investors who make appropriate representations. Generally, if an accredited investor cannot qualify as a “QIB” under Rule 144A, the seller will seek to use the Section 4(a)(1½) exemption for secondary sales of privately-held securities. See “What are the conditions that a reseller of restricted securities must satisfy to rely on Rule 144A?”.

Section 4(a)(1½) also is sometimes used to extend a Rule 144A offering to institutional accredited investors.

Source: The seminal case involving the so-called Section 4(a)(1½) exemption was the Second Circuit Court of Appeals decision in Gilligan, Will & Co. v. SEC, 267 F.2d 461 (2d Cir. 1959). The Second Circuit

intimated that a person purchasing restricted securities from an issuer is not an underwriter for purposes of Section 4(a)(1) if the purchaser resells the restricted securities to persons who qualify as purchasers under Section 4(a)(2) as described by the U.S. Supreme Court in SEC v. Ralston Purina Co., 346 U.S. 119 (1953), and who acquire the restricted securities in a private offering of the type contemplated by Section 4(a)(2).

Eligible Purchasers

What is a “QIB”?
In general, a QIB is any entity included within one of the categories of “accredited investor” defined in Rule 501 of Regulation D, acting for its own account or the accounts of other QIBs, that in the aggregate owns and invests on a discretionary basis at least $100 million in securities of issuers not affiliated with the entity ($10 million for a broker-dealer). See “Can the amount of securities to be purchased in a Rule 144A offering be included in calculating the amount of securities owned or invested by a QIB?”

In addition to the qualifications above, banks and savings and loan associations must have a net worth of at least $25 million to be deemed QIBs.

QIBs can be foreign or domestic entities, but must be institutions. Individuals cannot be QIBs, no matter how wealthy or sophisticated they are.

A broker-dealer acting as a riskless principal for an identified QIB would itself be deemed a QIB. To qualify as a riskless principal, the broker-dealer must have a commitment from the QIB that it will simultaneously purchase the securities from the broker-dealer. The
commitment from the QIB must be effective at the time of purchase in the Rule 144A transaction. A QIB may be formed merely for the purpose of investing in a Rule 144A transaction. See “Will an entity that is formed solely for the purpose of acquiring restricted securities in a Rule 144A transaction be deemed to be a QIB?”

How is the value of securities owned and invested by a QIB calculated under Rule 144A?

Typically, value is calculated on a cost basis (i.e., how much the securities cost when purchased). However, where the entity values securities on a fair market value basis for financial reporting purposes and no current information with respect to the cost of such securities has been published, the entity may use the fair market value basis for valuation. See “If a company reports both cost and mark-to-market values of the securities it holds, which values should be used to determine whether that company is a QIB?”

In determining the amount of securities, an entity may include securities of its consolidated subsidiaries if such securities are managed by that entity. However, unless an entity is a reporting company under the Exchange Act, securities owned by a subsidiary may not be included if the entity itself is a majority-owned subsidiary that would be included in the consolidated financial statements of another enterprise. In addition, an entity must exclude bank deposit notes, certificates of deposit, loan participations, repurchase agreements, and currency, interest rate, and commodity swaps. See “Can the amount of securities to be purchased in a Rule 144A offering be included in calculating the amount of securities owned or invested by a QIB?”

Source: Rule 144A(a)(2), (3) and (4) and SEC Compliance and Disclosure Interpretations, Securities Act Rules, Question 138.02 (Jan. 26, 2009), available at http://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm. For a detailed discussion of the securities that are included and excluded for purposes of determining whether a prospective purchaser is a QIB, see SEC No-Action Letter, UNUM Life Insurance Co. (available November 21, 1990).

If a company reports both cost and mark-to-market values of the securities it holds, which values should be used to determine whether that company is a QIB?

Only the cost valuation method should be used. The SEC staff has made clear its preference for cost valuation rather than market valuation when determining whether a prospective buyer is a QIB. This applies regardless of whether the company uses cost or mark-to-market financial reporting.


Can the amount of securities to be purchased in a Rule 144A offering be included in calculating the amount of securities owned or invested by a QIB?

No. The amount of securities to be purchased in a Rule 144A transaction may not be included when calculating the amount of securities that are owned or invested on a discretionary basis by a prospective purchaser for purposes of determining whether the purchaser is a QIB eligible to participate in the offering.

Source: SEC Compliance and Disclosure Interpretations, Securities Act Rules, Question 138.02 (Jan. 26, 2009), available at
Will an entity that is formed solely for the purpose of acquiring restricted securities in a Rule 144A transaction be deemed to be a QIB?

Yes. Eligible purchasers under Rule 144A can be entities formed solely for the purpose of acquiring restricted securities, so long as they satisfy the qualifying QIB tests.


How does a reseller establish a reasonable belief that a person is a QIB?

The reseller (and any person acting on the reseller’s behalf) may rely on the following, provided the information is as of a date not more than 16 months (18 months for a foreign purchaser) preceding the sale:

- the purchaser’s most recent publicly available annual financial statements;
- information filed with (a) the SEC, another U.S. federal, state or local governmental agency, or a self-regulatory organization, or (b) a foreign governmental agency or foreign self-regulatory organization;
- information in a recognized securities manual, such as Moody’s or Standard & Poor’s; or
- a certification by the purchaser’s chief financial or other executive officer specifying the amount of securities owned and invested as of a date on, or since, the end of the buyer’s most recent fiscal year.

This list is not exclusive. See “Can a reseller of restricted securities rely on information other than that enumerated in Rule 144A for its belief that the prospective purchaser is a QIB?”


Can a reseller rely on the information enumerated in Rule 144A even though more current information shows that the amount of securities owned by the prospective purchaser is lower?

Yes. The SEC has expressly stated so. However, a reseller cannot rely on certifications that it knows, or is reckless in not knowing, are false.


Can a reseller of restricted securities rely on information other than that enumerated in Rule 144A for its belief that the prospective purchaser is a QIB?

Yes. The bases for reliance enumerated in Rule 144A are non-exclusive; resellers may be able to establish a reasonable belief of eligibility based on factors other than those cited.

A reseller cannot rely on certifications that it knows, or is reckless in not knowing, are false. However, a seller has no duty of verification. In other words, unless the circumstances give a reseller reason to question the veracity of the information relied upon, the reseller does not have a duty to verify the information.


Effective September 2013, pursuant to Section 201 of the “Jumpstart Our Business Startups Act” (the “JOBS Act”), the SEC revised Rule 144A to permit general solicitation and general advertising of these offerings, provided that actual sales are only made to persons that
are reasonably believed to be “qualified institutional buyers.” As a result, issuers and underwriters now have enhanced flexibility to publicize a Rule 144A offering, without loss of the exemption from registration. The SEC has clarified that, in addition to the issuer, the initial purchasers and other distribution participants may conduct the general solicitation. (SEC Compliance and Disclosure Interpretations, Securities Act Rules, Question 138.03 (Nov 13, 2013)).

**Reseller’s Reasonable Steps So Buyer is Aware of Rule 144A Reliance**

**Why must the reseller take reasonable steps to make the purchaser aware that it is relying on Rule 144A in connection with the resale?**

The seller must make the purchaser aware that it is acquiring restricted securities since those securities may only be resold pursuant to an exemption from or registration under the Securities Act. The investor is entitled to know that the securities may be subject to reduced liquidity.

**How does the reseller typically satisfy the requirement of making the buyer aware that the reseller may rely on Rule 144A in connection with the resale?**

Typically, the warning is given by placing a legend on the security itself. For example, the note or stock certificate representing securities resold under Rule 144A will include a legend (or a notation for electronic records) stating that the securities have not been registered under the Securities Act and, therefore, may not be resold or otherwise disposed of in the absence of such registration or unless such transaction is exempt from, or not subject to, registration.

In addition, the private placement memorandum or other offering memorandum used in connection with the Rule 144A offering typically will include an appropriate notice to investors, such as the following:

“Each purchaser of the securities will be deemed to have represented and agreed that it is acquiring the securities for its own account or for an account with respect to which it exercises sole investment discretion, and that it or such account is a QIB and is aware that the sale is being made to it in reliance on Rule 144A.”

The offering memorandum also will advise the purchaser that the securities to be acquired can only be reoffered and resold pursuant to an exemption from, or registration under, the Securities Act.

Finally, the resold securities will have a restricted CUSIP number.

**Eligible Securities**

**What securities are eligible for exemption under Rule 144A?**

Securities offered under Rule 144A must not be “fungible” with, or substantially identical to, a class of securities listed on a national securities exchange (which includes the NASDAQ Market System) or quoted in an automated inter-dealer quotation system (“listed securities”). See “What happens if a security that was previously resold pursuant to Rule 144A is subsequently listed on a U.S. stock exchange or quoted on a U.S. automated inter-dealer quotation system?”

Common stock is deemed to be of the “same class” if it is of substantially similar character and the holders enjoy substantially similar rights and privileges.
American Depositary Receipts ("ADRs") are considered to be of the same class as the underlying equity security. See “Can a reseller rely on Rule 144A to reoffer or resell securities underlying ADRs?”

Preferred stock is deemed to be of the same class if its terms relating to dividend rate, liquidation preference, voting rights, convertibility, call, redemption, and other similar material matters are substantially identical.

Debt securities are deemed to be of the same class if the terms relating to interest rate, maturity, subordination, convertibility, call, redemption, and other material terms are substantially the same.

A convertible or exchangeable security with an effective conversion premium on issuance (which means at pricing) of less than 10%, and a warrant with a term less than three years or an effective exercise premium on issuance (at pricing) of less than 10%, will be treated as the “same class” as the underlying security. See “How is an effective conversion premium calculated?” below.

Source: Rule 144A(d)(3)(i) and SEC Release No. 33-6862 (April 23, 1990). Rule 144A(d)(3)(i) “invites a comparison of apparently different types of securities of the same issuer to determine whether in reality they should be considered the same class.” J. William Hicks, Resales of Restricted Securities at 7-18 (West Group 2007). The SEC has stated that privately placed securities that, at the time of issuance, were fungible with securities trading on a U.S. exchange or quoted in NASDAQ would not be eligible for resale under Rule 144A. In Release No. 33-6862 (April 23, 1990), the SEC stated that the test under Rule 144A to determine whether common stock will be deemed to be of the same class is the same as the test used under Section 12(g)(5) of the Exchange Act (which governs the requirement to register a class of securities under the Exchange Act) and will be interpreted by the SEC in the same manner.

How is an effective conversion premium calculated?
For a convertible security, by (a) taking its price at issuance, (b) subtracting from such price the aggregate market value of the securities that would be received on conversion, and (c) dividing the difference by the amount subtracted in (b).

For a warrant, by (a) taking its price at issuance, (b) adding to such price its aggregate exercise price, (c) subtracting from such number the aggregate market value of the securities that would be received on exercise, and (d) dividing the difference by the amount subtracted in (c).

For both of these calculations, the market value of the underlying securities is determined as of the day of pricing of the convertible security or warrant.

Source: Notes 25 and 26 of SEC Release No. 33-6862 (April 23, 1990) provide examples showing how to calculate the effective conversion premium and effective exercise premium.

Are restricted securities received upon conversion eligible for resale even though they are the same class as securities listed on a national securities exchange or quoted in an automated inter-dealer quotation system?
Yes, but only if no additional consideration is paid by the holder in connection with such conversion. Thus, restricted securities received upon conversion without payment of additional consideration by the holder, where the convertible securities are eligible for resale under Rule 144A, may be resold in reliance on Rule 144A.
Can a reseller rely on Rule 144A to reoffer or resell securities underlying ADRs?

No. If American Depositary Receipts are listed on a U.S. national securities exchange or quoted on an automated inter-dealer quotation system, the deposited securities underlying the ADRs also would be considered publicly traded, and may not be resold in reliance on Rule 144A.


What happens if a security that was previously resold under Rule 144A is subsequently listed on a U.S. stock exchange or quoted on a U.S. automated inter-dealer quotation system?

There is no effect on the eligibility of previously issued Rule 144A securities. Eligibility under Rule 144A is determined at the time of issuance, so securities of the same class that thereafter are listed on a U.S. national securities exchange or a U.S. automated inter-dealer quotation system will not affect the eligibility of the securities under the rule.

Source: In SEC Release No. 33-6839 (July 19, 1989), the SEC stated that “eligibility for resale [under Rule 144A] would be determined at the time of issuance in interest of certainty.” See also SEC No-Action Letter Shearman & Sterling (December 21, 1998).

Informational Requirements

What type of information is required to be delivered to purchasers under Rule 144A?

To satisfy Rule 144A, if the issuer is not (1) a reporting company under the Exchange Act, (2) a foreign company exempt from reporting under Rule 12g3-2(b), or (3) a foreign government, the holder of the securities and any prospective purchaser designated by the holder must have the right to obtain from the issuer, upon request of the holder, the following information:

- a brief description of the issuer’s business, products, and services;
- the issuer’s most recent balance sheet, profit and loss statement, and retained earnings statement (the financial statements must be audited if audited statements are “reasonably available”); and
- similar financial statements for the two preceding fiscal years.

The information must be “reasonably current” in relation to the date of resale under Rule 144A. See “What does ‘reasonably current’ information mean in connection with furnishing disclosure to purchasers?”

This delivery obligation can continue for some time. See “When does the obligation to provide a buyer with the information cease?”

In addition to this information requirement, in connection with an initial offering of Rule 144A securities, the issuer and the initial purchaser(s) typically will prepare an offering memorandum relating to the issuer and the securities. See “What type of documentation is typically involved in a Rule 144A transaction?” The disclosure in the offering memorandum, or incorporated by reference in the offering memorandum, will typically exceed the amount of disclosure that is required to be made available under Rule 144A. This is because the offering memorandum often is used as a marketing document, and because having robust disclosure of the issuer’s
business, finances, and securities helps reduce the potential liabilities of the issuer and the initial purchasers for violations of the U.S. securities laws. See “Are the antifraud provisions of the federal securities laws applicable to Rule 144A transactions?”

Source: Rule 144A(d)(4)(i).

What does “reasonably current” information mean in connection with furnishing disclosure to purchasers?

To be reasonably current:

- the business description must be as of a date within 12 months prior to the resale;
- the most recent balance sheet must be as of a date within 16 months prior to the resale; and
- the most recent profit and loss and retained earnings statements must be for the 12 months preceding the date of the balance sheet.

For a foreign issuer, if the required information meets the timing requirements of its home country or principal trading markets, such information will be presumed to be reasonably current. See “What type of information needs to be provided by an Exchange Act reporting company or a foreign issuer providing home country information?”

Source: Rule 144A(d)(4)(ii).

How is the purchaser’s “right to obtain” such information from the issuer established?

Rule 144A does not specify the manner by which the right to obtain information would arise. Typically, the issuer’s obligation to furnish information will be imposed by either:

- the terms of the security, such as a covenant in a paying agency agreement, form of note, or certificate of designations for preferred stock; or
- a purchase agreement or other contract between the issuer and the initial purchasers of the Rule 144A securities.

What type of information needs to be provided by an Exchange Act reporting company or a foreign issuer providing home country information?

An issuer that is subject to the reporting requirements of Section 13 or 15(d) of the Exchange Act, or exempt from reporting pursuant to Rule 12g3-2(b) under the Exchange Act, is not subject to the requirement to furnish information under Rule 144A.

In the case of foreign private issuers (which are permitted to furnish home country information under Rule 12g3-2(b)), the requirement to be “reasonably current” will be satisfied if the required information meets the time requirements of the issuer’s home country or principal trading markets.

Source: Rule 144(d)(4)(ii)(C).

When does the obligation to provide a buyer with the information cease?

The obligation to provide information continues so long as the issuer is neither a reporting company nor a foreign issuer providing home country information.

What information is required to be provided to a buyer when a Rule 144A issuer’s securities are guaranteed by its parent company?

It depends on the status of the parent-guarantor. The information requirement does not apply if the securities are guaranteed by a parent company that would itself be exempt from the information requirement. If the
parent-guarantor is not exempt, the information to be supplied is that of the parent-guarantor.

Source: The staff’s position comes from the SEC No-Action Letters British Aerospace (available May 9, 1990) and Schering-Plough Corp (available November 21, 1991).

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**Rule 144A Trading Markets**

*Is there a trading market for Rule 144A securities?*

Yes to an extent, and equity and debt securities trade differently. Since the enactment of Rule 144A, there have been a number of alternative markets that were developed but never became firmly established, the best known being the PORTAL market. PORTAL, which stood for “Private Offerings, Resale and Trading through Automated Linkages,” was NASDAQ’s screen-based automated trading system for Rule 144A securities. In November 2007, a consortium of investment banks, in conjunction with NASDAQ, created the PORTAL Alliance for trading unregistered securities on a single platform. The PORTAL Alliance is a closed trading market that limits trading to qualified institutions and established depositary and clearance systems so that trades can only be made to other such institutions, or outside the United States, or pursuant to a registration statement or exemption from registration. The PORTAL Alliance’s founding members were BofA Merrill Lynch, Citi, Credit Suisse, Deutsche Bank, Goldman Sachs, J.P. Morgan, Morgan Stanley, The NASDAQ OMX Group, Inc., UBS and Wells Fargo Securities. The Portal Alliance mainly trades equity securities. In recent years, a number of private secondary trading markets, primarily for equity securities, have also developed, including SecondMarket and SharesPost. These markets typically give accredited investors access as well as QIBs. It is unclear how all these private secondary markets will adapt to the 2013 termination of the prohibition on general solicitation.

In 2009, the SEC approved changes to procedures of The Depository Trust Company (known as DTC), which, among other things, provides clearing and settlement services, to permit greater liquidity in the trading of Rule 144A securities. Prior to the rule change, Rule 144A securities, other than investment grade securities, were eligible for DTC’s deposit, book-entry delivery, and other depository services provided, in part, that such securities were included in an “SRO Rule 144A System” (frequently referred to as the “SRO Requirement”), such as the PORTAL. Following the rule change, DTC eliminated the SRO Requirement, thereby creating a uniform procedure for making all Rule 144A securities DTC-eligible. Issuers and participants continue to be responsible for determining that their deposit of Rule 144A securities at DTC and their transactions in Rule 144A securities through DTC’s facilities are in compliance with existing DTC rules and the federal securities laws.

*Are Rule 144A transactions subject to FINRA’s TRACE reporting system?*

Yes. In 2014, FINRA adopted new rules relating to its Trade Reporting and Compliance Engine (“TRACE”). Revised Rule 6750 includes Rule 144A transactions among the transactions about which FINRA disseminates information upon receipt of a transaction report from a broker dealer. Revised FINRA Rule 7730 establishes a real-time market data set for Rule 144A transactions, as well as a historical data set. These
Conducting Rule 144A Transactions

How are Rule 144A transactions structured?

Typically, an issuer first sells restricted securities to a broker-dealer (often referred to as an “initial purchaser”) in a private placement exempt from registration under Section 4(a)(2) or, less frequently, Regulation D of the Securities Act. The broker-dealer then reoffers and resells the securities to QIBs using the exemption provided by Rule 144A. See “What are the conditions that a reseller of restricted securities must satisfy to rely on Rule 144A?” and “What is a ‘QIB?’”

Rule 144A permits the broker-dealer to immediately reoffer and resell the restricted securities, even though it has purchased the securities with a view to their distribution. The availability of Rule 144A does not depend on how much time has expired since the securities were issued or on whether the reseller had an investment intent when it purchased the securities.

Resales under Rule 144A are completely separated from the issuer’s original offering—no matter how soon they occur or how inconsistent they are with the issuer’s exemption. In this regard, Rule 144A states that resales “shall be deemed not to affect the availability of any exemption or safe harbor relating to any previous or subsequent offer or sale of such securities by the issuer.”

Source: Preliminary Note No. 7 to Rule 144A, and Rule 144A(e).

What type of documentation is typically involved in a Rule 144A transaction?

The documentation used in a Rule 144A transaction is similar to that used in registered offerings, including:

- an offering memorandum;
- a purchase agreement between the issuer and the initial purchasers (i.e., broker-dealers);
- in some cases, a registration rights agreement between the issuer and the initial purchasers;
- legal opinions; and
- comfort letters.

The offering memorandum typically will contain a detailed description of the issuer, including its financial statements, and the securities to be offered. In the case of a publicly traded issuer, the offering memorandum may incorporate by reference the issuer’s Exchange Act filings instead of reproducing the disclosure.

The form, organization, and content of a purchase agreement for a Rule 144A offering often resembles an underwriting agreement for a public offering in many respects, but is modified to reflect the manner of offering.

In the case of a Rule 144A offering that is combined with a Regulation S offering, the Regulation S offering may be conducted using documents that are based on the country-specific practices of the relevant non-U.S. jurisdiction or jurisdictions. However, the disclosure documents in such a case generally will contain the same substantive information so that investors have the same “disclosure package.”

In connection with offerings of debt securities, it is very common to have a Rule 144A tranche offered to QIBs, and a Regulation S tranche offered to non-U.S.
persons. However, while Rule 144A securities generally have a restricted period of six months to one year, Regulation S debt securities have a restricted period of only 40 days. Therefore, these tranches are represented by separate certificates in order to help ensure their lawful transfer in the secondary market. In such a case, the Rule 144A global certificate with a Rule 144A restrictive legend is deposited with DTC, while the Regulation S global certificate with a Regulation S restrictive legend is deposited with a European clearing system. These two securities have different CUSIP numbers and other security identification numbers. The Rule 144A securities can be re-sold to non-U.S. persons if the buyer certifies that it is not a U.S. person, and the sale otherwise complies with Regulation S. The Regulation S securities can be re-sold in the United States to QIBs if the resale complies with Rule 144A. In each such case, the registrar for the securities will make appropriate entries to reflect increases or decreases in the respective certificates.

Note: A registration rights agreement would only be applicable to Rule 144A transactions in which the issuer has agreed to register under the Securities Act the securities resold in the Rule 144A transaction. See “How are Rule 144A securities registered under the Securities Act?”

What is the offering process in connection with a Rule 144A transaction?

The Rule 144A offering process is often similar to the public offering process. The features of this process typically include:

- solicitation of orders using a “red herring” or preliminary offering memorandum;
- preparation and delivery of a final term sheet to investors to indicate the final pricing terms;
- confirmation of orders using a final offering memorandum;
- execution of the purchase agreement at pricing;
- delivery of the comfort letter from the issuer’s auditing firm at pricing;
- delivery of legal opinions and other closing documents at closing; and
- closing three to five days after pricing.

See “What type of documentation is typically involved in a Rule 144A transaction?”

How does Rule 159 under the Securities Act impact the Rule 144A market?

Rule 159 was adopted by the SEC in 2005 as part of the SEC’s “Securities Offering Reform” rules. Rule 159 restates the SEC Staff’s traditional position that, for purposes of determining the adequacy of the disclosure in a prospectus, such adequacy would be evaluated as of the time that an investor formed a contract to purchase the securities.

In the U.S. securities market, the purchase contract usually precedes delivery of the final prospectus. Accordingly, after Rule 159 was adopted, a market practice developed in registered offerings—particularly debt offerings—under which the issuer or the underwriters provide to investors a final term sheet or similar document at the time of pricing that conveys to the investor the information that was not included in the preliminary prospectus. Typically, this information consists solely of pricing-specific information, such as the aggregate principal amount and the interest rate of
debt securities. However, such a document could include other information, such as corrections to the preliminary prospectus or a description of recent developments in the issuer’s business. (The document that contained this information would typically be a “free writing prospectus” under Securities Offering Reform rules.) The forms of legal opinions and officer certificates also were updated to refer to the adequacy of the so-called “disclosure package” as of the “initial sale time.”

Technically, Rule 159 only applies in the context of a registered public offering. However, many practitioners became concerned that, if a court ever tested the accuracy of a preliminary Rule 144A offering memorandum as of the time of pricing, based upon the principles set forth in Rule 159 and its rationale, the disclosure could be found deficient. Accordingly, some of the pricing practices in connection with registered offerings were adapted to the Rule 144A market, such as the delivery of term sheets, and required statements in legal opinions and officer certificates.

Why should initial purchasers conduct a due diligence investigation in connection with a Rule 144A offering?

A due diligence investigation is a critical component in an initial purchaser’s decision whether to undertake an offering, enabling the prospective purchaser to evaluate the relevant legal, business, and reputational risks.

Rule 144A offerings do not subject the issuer and the initial purchasers to liability under Section 11 of the Securities Act. Accordingly, the initial purchasers are not entitled to the “due diligence” defense that may be established under Section 11. Nonetheless, a thorough due diligence investigation by lawyers, accountants, the issuer, and the underwriter generally will result in better disclosure and a lower risk of liability or potential liability for material misstatements or omissions.

What is the due diligence process for initial purchasers in connection with a Rule 144A offering?

The Rule 144A due diligence process is similar to that followed in connection with registered public offerings. Generally, the due diligence process is divided into two parts: (a) business and management due diligence, and (b) documentary, or legal, due diligence. In order to help establish their due diligence, the initial purchasers in a Rule 144A offering often will receive documents at closing that are similar to those used in an underwritten offering, including a comfort letter, legal opinions, and officer certificates.

Why do Rule 144A purchasers often insist that the issuer register the securities issued in the Rule 144A transaction?

Liquidity is the primary benefit that comes from holding freely tradable securities rather than restricted securities. See “Are securities resold under Rule 144A freely tradable after such resale?” In addition, certain state and federal laws prohibit some mutual funds and insurance companies from investing more than a certain percentage of their assets in restricted securities. Some investment partnerships and similar entities are subject to comparable restrictions under their organizational documents. Absent an issuer’s agreement to register Rule 144A securities, these entities would be severely limited in their ability to purchase securities in Rule 144A transactions.

Since the holding period under Rule 144 for securities issued by reporting companies was reduced effective February 2008 from one year to six months (see “What are the holding periods applicable to the sale of Rule
144A and other restricted securities?"), there is a shorter period of time after the contractual deadline in which non-affiliated investors are restricted from selling the securities under Rule 144, which generally decreases the need for registration rights and, as a consequence, limit the incremental value that registration rights previously provided.

**How are Rule 144A securities registered under the Securities Act?**

The two principal methods to register Rule 144A securities under the Securities Act are:

- "Exxon Capital" exchange offers (see “What is an Exxon Capital exchange offering?"), and
- Shelf registrations under Rule 415 of the Securities Act. (see “How are Rule 144A securities registered in a ‘shelf offering?’").

**What is an Exxon Capital exchange offering?**

An Exxon Capital exchange offering is a procedure under which securities are privately placed under Rule 144A and then promptly exchanged for similar securities that have been registered under the Securities Act. This is generally the preferred means for providing holders of Rule 144A securities with freely tradable securities.

From the issuer’s standpoint, an Exxon Capital exchange offer eliminates the need to continuously update a shelf registration statement over its lifetime if any of the investors in the Rule 144A offering are affiliates of the issuer. However, these exchange offers currently are permissible only with respect to non-convertible debt securities, investment grade preferred stock, and initial public offerings of common stock by foreign issuers conducted under Rule 144A. Moreover, affiliates of the issuer may not participate in an Exxon Capital exchange offer, and the SEC takes the position that broker-dealers also may not participate in these exchange offers. In addition, all exchanging holders will be required to represent that they acquired the securities in the ordinary course of their business and have no arrangements or understandings with respect to the distribution of the security that is the subject of the exchange offer. The SEC has indicated that it is unlikely to expand the permissible scope of these exchange offers beyond the current parameters. See “Why are shelf offerings not the preferable form of registering Rule 144A offerings?”

**Source:** The SEC staff’s positions in this area come from a series of no-action letters: Exxon Capital Holding Corp. (available May 13, 1988); Morgan Stanley & Co. Incorporated (available June 5, 1991); K-III Communications Corporation (available May 14, 1993); and Shearman & Sterling (available July 2, 1993).

**How are Rule 144A securities registered in a shelf offering?**

Under Rule 415(a)(1)(i) of the Securities Act, issuers of Rule 144A securities may register the resale of the restricted securities that were sold in the Rule 144A transaction. Registered offerings under Rule 415 are known as shelf registrations.

Rule 415(a)(1)(i) permits either a delayed or continuous offering of securities “which are to be offered or sold solely by or on behalf of a person or persons other than the registrant . . . .” The persons covered by this rule would include resellers holding Rule 144A securities.

Although shelf registrations offer potential liquidity to buyers of Rule 144A securities, the securities remain
restricted until they are resold under the shelf registration statement. In shelf registrations, the issuer should covenant to keep the shelf registration statement continuously effective for no less than one year in order to ensure the holder liquidity until the resale exemption under Rule 144 becomes available without any limitations on non-affiliates.

Why are shelf offerings not the preferable form of registering Rule 144A offerings?

If Rule 144A securities are held in book-entry form at DTC, preparation of shelf registration statements can be extremely difficult from an administrative perspective.

The SEC requires that the prospectus contain a list of the beneficial owners of the restricted securities that will be resold using the shelf registration statement. However, when securities are uncertificated, it is virtually impossible to identify the beneficial owner for whom the registered holder (i.e., CEDE & Co., as DTC’s nominee) holds the securities, especially after the securities have been transferred by their initial holders. As a result, an issuer typically will require that holders of Rule 144A securities notify it regarding any resales of the securities, and that new holders of the securities furnish a notice and questionnaire before they can be added to the registration statement.

Because of these administrative issues, Exxon Capital exchange offers are the preferred means for providing holders of Rule 144A securities with freely tradable securities. See “What is an Exxon Capital exchange offering?”

Use of the Internet to Conduct Rule 144A Offerings

Can the Internet be used to make Rule 144A reoffers and resales?

Prior to the September 2013 revision of Rule 144A that permitted general solicitation, the SEC permitted road shows in connection with a Rule 144A offering to be made over the Internet to QIBs. See “What is a ‘QIB?’” Access to the road show was password-protected, with a separate password for each offering. Passwords were issued only to those potential purchasers the seller reasonably believes are QIBs, and the seller must not otherwise have had knowledge or reason to believe that any such potential purchaser is not a QIB.

The SEC had issued a no-action letter permitting sellers to rely on a third-party vendor’s Internet-based list of QIBs, which must be certified by such vendor(s).

Effective September 2013, the SEC revised Rule 144A to permit general solicitation and general advertising of these offerings, provided that actual sales are only made to persons that are reasonably believed to be QIBs. Accordingly, these limitations no longer apply to Rule 144A offerings, and an unrestricted website may serve as a viable mechanism to offer Rule 144A securities. Of course, any broker effecting sales in such an offering will need to take steps to ensure that it sells only to QIBs.

FINRA Filing Requirements

Are Rule 144A offerings subject to filing under FINRA’s Corporate Financing Rule?

No. Rule 144A offerings are exempt from this filing requirement.

Source: FINRA Rule 5110(b)(1) and 5110(b)(8)(A).

Are Rule 144A offering documents subject to filing with FINRA as “private placements”?

No. Offerings to QIBs are exempt from FINRA’s requirement to file private placement documents.

Source: FINRA Rule 5123(b)(3).

Other Issues

Are the antifraud provisions of the federal securities laws applicable to Rule 144A transactions?

Yes. Preliminary Note No. 1 of Rule 144A specifically states that the safe harbor provided by the rule relates solely to the application of Section 5 of the Securities Act and not to the antifraud provisions.

Because the antifraud provisions apply to Rule 144A transactions, an offering memorandum typically contains information comparable to what a prospectus for a registered offering would contain.

Is a Rule 144A security a “covered security” for purposes of Section 18 of the Securities Act?

It depends. Section 18 of the Securities Act exempts certain securities and securities offerings from state regulation relating to registration or qualification of securities or securities transactions. However, states may continue to require notice filings to be made in connection with exempt securities or offerings.

Section 18 will exempt Rule 144A transactions from state regulation if (i) the issuer of the securities being resold in the Rule 144A transaction has a class of securities traded on the New York Stock Exchange, American Stock Exchange, or the NASDAQ Market System, and (ii) the securities being resold in the Rule 144A transaction are equal or senior to the issuer’s securities that are listed on one of the above-referenced markets. For example, if an issuer has common stock traded on the New York Stock Exchange, and it offers senior debt securities in a Rule 144A offering, the debt securities will be “covered securities” under Section 18.

In addition, Section 18 will exempt from state regulation Rule 144A resales to a “qualified purchaser.” In December 2001, the SEC issued a proposed rule to define the term “qualified purchaser” for purposes of Section 18, but the proposed rule was never adopted. The proposed definition mirrors the definition of “accredited investor” under the Securities Act, but since the SEC never formally adopted the definition, most legal practitioners are reluctant to advise their clients that they may rely on it or, consequently, on this provision of Section 18.

If Section 18 does not exempt the Rule 144A transaction from state regulation, then the transaction will be required to be registered with each state in which the Rule 144A resales occur or must otherwise be exempt from such state registration. Most state securities laws contain an exemption from registration for reoffers and resales made to QIBs within the meaning of Rule 144A. In states that do not have the specific exemption, Rule 144A sales often are exempt because Rule 144A purchasers would likely be deemed...
to be “institutional investors” for purposes of such states’ analogous institutional investor exemption.

Source: Preliminary Note No. 5 of Rule 144A and SEC Release No. 33-6862 (April 23, 1990) state that nothing in Rule 144A removes the need to comply with any applicable state law relating to the offer and sale of securities. See Section 18(b)(1)(C) with respect to the covered security exemption, and Section 18(b)(3) with respect to the “qualified purchaser” exemption.

Can an issuer that is not an Exchange Act reporting company be required to register under the Exchange Act in connection with a Rule 144A transaction?

Yes. An issuer must register under Section 12(g) of the Exchange Act if a class of its equity securities (other than exempted securities) is held of record by either (i) 2,000 persons, or (ii) 500 persons who are not accredited investors and, on the last day of the issuer’s fiscal year, its total assets exceed $10 million (or, in the case of a bank holding company, if it had total assets that exceeded $10,000,000 and a class of equity securities held of record by 2,000 or more persons). The “held of record” definition in Section 12(g)(5) does not include securities received by the holder pursuant to an employee compensation plan in exempt transactions under Section 5 of the Securities Act or in a crowdfunding offering. Note that foreign private issuers may qualify for exemptions to such registration requirements. See our Frequently Asked Questions About Foreign Private Issuers, available at http://www.mofo.com/files/Uploads/Images/100521FAQForeignPrivate.pdf.

As a result, a non-reporting company that has sold equity securities in connection with a Rule 144A transaction may be required to register that class of equity securities. This may occur as a result of resales of the Rule 144A securities in the secondary market, other transactions that increase the number of holders, or, in the case of a foreign private issuer, a listing on NASDAQ. Companies that effect “backdoor IPOs” under Rule 144A must be careful to monitor the number of their equity holders.

Source: Rule 12g3-2(a). Preliminary Note No. 4 of Rule 144A and SEC Release No. 33-6862 (April 23, 1990) state that Rule 144A does not affect the securities registration requirements of Section 12 of the Exchange Act.

Are securities resold in reliance on Rule 144A included in determining the amount of securities that a person can resell in reliance on Rule 144?

No. Securities resold in reliance on Rule 144A need not be included in determining the amount of securities that can be resold in reliance on Rule 144.


May an issuer publish a notice about a proposed Rule 144A transaction?

Yes. An offering under Rule 144A is an unregistered offering within the meaning of Rule 135c of the Securities Act. An issuer that is subject to the reporting requirements of the Exchange Act or that is exempt from these reporting requirements under Rule 12g3-2(b) is entitled to rely on Rule 135c to publish a notice that it proposes to make, is making, or has made an offering of securities in a Rule 144A transaction. In addition, Rules 168 and 169 provide a safe harbor for regularly released factual business information, including information maintained on a company’s website.
As a result of the JOBS Act, issuers are now also permitted to broadly disseminate a press release regarding a proposed or completed Rule 144A offering without forfeiting the exemption from registration.

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FREQUENTLY ASKED QUESTIONS ABOUT RULE 144A EQUITY OFFERINGS

These FAQs relate specifically to Rule 144A equity offerings. Please refer to our Frequently Asked Questions About Rule 144A generally, and our Frequently Asked Questions About Initial Public Offerings for additional information about equity offerings.

Understanding Rule 144A Equity Offerings

What is a Rule 144A equity offering?

A Rule 144A equity offering is an unregistered offer and sale of equity securities issued by a U.S. or foreign company, the equity securities of which are neither listed on a U.S. securities exchange nor quoted on a U.S. automated inter-dealer quotation system. See “Frequently Asked Questions About Rule 144A—What securities are eligible for exemption under Rule 144A?”

Rule 144A under the Securities Act of 1933, as amended (the “Securities Act”), provides a non-exclusive safe harbor from the registration requirements of Section 5 of the Securities Act for certain offers and sales of qualifying securities by certain persons other than the issuer of the securities. A Rule 144A equity offering is usually structured so that the issuer first sells newly issued securities to an “initial purchaser,” typically a broker-dealer, in a private placement exempt from registration under the Securities Act. The initial purchaser can then take advantage of the Rule 144A safe harbor to reoffer and resell the restricted securities immediately to qualified institutional buyers (“QIBs”).

Rule 144A provides that reoffers and resales in compliance with the rule are not “distributions” and, therefore, the reseller is not an “underwriter” within the meaning of Section 2(a)(11) of the Securities Act. A reseller that is not the issuer, an underwriter, or a dealer can rely on the exemption provided by Section 4(a)(1) of the Securities Act. Resellers that are dealers can rely on the exemption provided by Section 4(a)(3) of the Securities Act.

Which securities are eligible for exemption under Rule 144A?

Equity securities offered pursuant to Rule 144A, when issued, must not be “fungible” with or substantially identical to a class of securities listed on a national securities exchange or quoted in an automated inter-dealer quotation system (“Listed Securities”). Common stock is deemed to be of the “same class” if it is of substantially similar character and the holders enjoy substantially similar rights and privileges. American Depositary Receipts (“ADRs”) are considered to be of
the same class as the underlying equity security. Preferred stock is deemed to be of the same class if the terms of the preferred stock relating to dividend rate, liquidation preference, voting rights, convertibility, call, redemption, and other similar material matters are substantially identical. A convertible or exchangeable security with an effective conversion premium upon issuance (at pricing) of less than 10%, and a warrant with a term of less than three years or an effective exercise premium on issuance (at pricing) of less than 10%, will be treated as the “same class” as the underlying security. See also “Frequently Asked Questions About Rule 144A—Eligible securities.”


The Securities and Exchange Commission (“SEC”) has stated that privately placed securities that, at the time of issuance, were fungible with securities trading on a U.S. exchange or quoted on NASDAQ would not be eligible for resale under Rule 144A. In Release No. 33-6862 (April 23, 1990), the SEC stated that the test under Rule 144A to determine whether common stock will be deemed to be of the same class is the same as the test used under Section 12(g)(5) of the Exchange Act of 1934, as amended (the “Exchange Act”) (which section governs the requirement to register a class of securities under the Exchange Act) and will be interpreted by the SEC in the same manner.

In addition to the foregoing, Rule 144A does not cover resales of securities issued by open-end investment companies, unit investment trusts, and face-amount certificate companies that are required to be registered under Section 8 of the Investment Company Act of 1940.

Source: Rule 144A(d)(3)(ii).

Who may rely on Rule 144A?

Issuers are not eligible to rely on Rule 144A for the sale of securities. Rather, in a Rule 144A equity offering, issuers rely on any valid exemption for the offer and sale of unregistered securities when they sell securities to the initial purchaser(s). Often issuers rely on Section 4(a)(2) or Regulation D, or Regulation S under the Securities Act. The initial purchaser(s), or any person or entity other than the issuer, may rely on Rule 144A for the resale of the securities. Generally, the initial purchaser are broker-dealers. Affiliates of the issuer may rely on Rule 144A.


Why conduct a Rule 144A equity offering?

Privately held companies may find a Rule 144A equity offering to be an attractive alternative to an IPO, especially if the IPO market is closed. The market often views an equity 144A offering as a stepping stone to an IPO. An issuer can complete a Rule 144A offering while waiting for the IPO window to open. The preparations for a Rule 144A equity offering are substantially similar to those for an IPO, though less involved. Also, an issuer that has commenced the IPO process can leverage all of that work, and quickly and efficiently use many of the disclosures prepared in connection with an IPO for a Rule 144A equity offering. If the IPO window opens
before or even after the closing of the Rule 144A offering, the work undertaken in connection with the Rule 144A equity offering can easily and effectively be leveraged for the IPO. Other, alternative offerings that an issuer may consider while the IPO window is closed are less favorable for the issuer.

The ability to resell securities in reliance on Rule 144A enables broker-dealers to structure offerings that closely resemble traditional firm commitment public offerings. Once the securities are in the hands of QIBs, a market for the securities may develop among QIBs. These markets do not provide the same liquidity as national securities exchanges but they provide some liquidity nonetheless. The issuer can enhance the liquidity of the securities by including its securities in one of the trading markets for restricted securities. In many Rule 144A equity offerings, the issuer agrees to commence an IPO or to register the offered securities for resale within a fixed period of time.

Foreign issuers that do not want to become subject to U.S. reporting requirements may also be interested in Rule 144A equity offerings.

In addition to providing yet another capital-raising alternative, a Rule 144A equity offering offers other benefits. Issuers in a Rule 144A offering have greater flexibility with respect to disclosure than do issuers in a public offering. Although issuers generally produce offering memoranda that include SEC-style disclosure, the contents of the offering memoranda are dictated by industry practice, not SEC regulation. Issuers are not required to comply with the regulations that prescribe the disclosure requirements for the registration statements used in public offerings. Further, there is no SEC review of the offering memorandum, thus eliminating the delay associated with SEC review. Until the issuer becomes an SEC reporting company, it is not subject to the corporate governance provisions of the federal securities laws and the national securities exchanges, nor is it exposed to the liabilities arising from these provisions, particularly those set forth in the Sarbanes-Oxley Act. See “What Are The Disclosure Requirements For Rule 144A Equity Offerings?”

Finally, many Rule 144A offerings are structured as global offerings, with a side-by-side offering targeted at foreign holders in reliance on Regulation S. This dual structure permits an issuer, especially a foreign issuer, to broaden its potential pool of investors. A foreign issuer may take advantage of this structure to attract investors from its home country that are already familiar with the issuer.

**What are the advantages of undertaking a Rule 144A equity offering?**

In addition to the potential efficiencies that may be realized by a private company that completes a Rule 144A equity offering prior to completing an IPO, the advantages of a Rule 144A offering, include: (1) no public disclosure of innovative structures or sensitive information; (2) limited (or no) FINRA filing requirements, and (3) reduced for liability under the Securities Act. See “Why Conduct a Rule 144 Equity Offering?”

**What are the disadvantages of conducting a Rule 144A equity offering?**

Rule 144A offerings are limited to QIBs, which limits the universe of potential purchasers. Following the completion of the offering, there will not be an immediate, liquid secondary market for the offered securities. See “Frequently Asked Questions About Rule 144A—Are securities resold under Rule 144A...”
freely tradable after such resale?” Investors may demand a liquidity discount for the offered securities.

A Rule 144A offering may allow a private company to raise capital from institutional investors and become better known; however, it is unlikely to result in any research analyst following. The company will defer becoming subject to SEC reporting requirements, but Rule 144A issuers are required to provide purchasers, at their request, with reasonably current information. See “What Are the Disclosure Requirements For Rule 144A Equity Offerings?”

A non-reporting issuer that conducts a Rule 144A equity offering also must monitor the number of its equity holders to ensure that it does not inadvertently become subject to SEC reporting requirements by crossing the holder of record threshold. It does not matter how the equity holder acquired its interests in the issuer. Accordingly, an issuer may limit an offering to a small number of initial purchasers for purposes of avoiding the reporting rules but eventually become subject to the reporting requirements if ownership of its securities becomes more dispersed. The number of holders can be monitored relatively easily by a transfer agent or through the facilities of a private secondary trading market.

As discussed above, equity securities offered under Rule 144A must not be fungible with, or substantially identical to, listed securities. Accordingly, it is not likely that an issuer will be able to complete multiple Rule 144A equity offerings.

What are the principal steps for a Rule 144A equity offering?
An issuer first sells restricted securities to one or more initial purchasers in a private placement exempt from registration, generally under Section 4(a)(2), and/or Regulation D, or Regulation S of the Securities Act. The initial purchasers will be broker-dealers. The broker-dealers reoffer and resell the securities to QIBs in reliance on the Rule 144A resale safe harbor.

What are the disclosure requirements for Rule 144A equity offerings?
There are no regulations prescribing the disclosure requirements for a Rule 144A offering. Most practitioners advise their clients to prepare an offering memorandum that contains substantially the same issuer type of information that an issuer would be required to include in a registration statement. Moreover, if the issuer is preparing for a future IPO, it will need to prepare audited financial statements. However, it is important to note that, market practice aside, the issuer will have significant flexibility regarding the presentation of information in the offering memorandum. For example, the issuer may choose to present summary or selected information for fewer years or may include limited executive compensation information in the offering memorandum.

Once an issuer has commenced the Rule 144A offering process, Rule 144A requires that issuers provide purchasers, at their request, with “reasonably current” information about the issuer unless the issuer is (i) not a reporting company under the Exchange Act, (ii) a foreign issuer exempt from reporting pursuant to Rule 12g3-2(b) of the Exchange Act, or (iii) a foreign government.

Such information includes the following:

- A brief description of the issuer’s business, products, and services;
• The issuer’s most recent balance sheet, profit and loss statement, and retained earnings statement; and

• Any similar financial statements for such part of the two preceding fiscal years as the issuer has been in operation (the financial statements must be audited if audited statements are “reasonably available”).

With respect to a foreign private issuer (as defined under the U.S. federal securities laws), information will be presumed reasonably current if the information meets the timing requirements of the issuer’s home country or principal trading market.

The obligation to provide information to purchasers continues so long as the issuer is neither a reporting company nor a foreign issuer providing home country information.

Who is involved in a Rule 144A equity offering?

The participants in a Rule 144A equity offering include many of the same players as would be involved in an IPO. Retaining the proper external advisers is important for a successful offering. The offering team will include one or more initial purchasers. The initial purchasers may be the same broker-dealers that would serve as underwriters in an IPO by the same issuer. If there are multiple initial purchasers, one may serve as the lead and the others may play the same role as co-managers of an IPO. Also involved (although technically not required), is an independent auditing firm with significant public company experience and outside legal counsel. Financial printers are not required but should be considered, depending on the size of the offering. A transfer agent is not required, assuming the issuer is not yet public, but the issuer should be ready to engage a transfer agent by the time any registration statement is filed, if contemplated. An issuer may also want to hire an investor relations firm.

An issuer should also have an internal offering team in place. Key members of the internal team should include the issuer’s president, CEO, CFO, general counsel, controller, and an investor relations or public relations manager. Depending on the issuer’s industry, other team members may be essential. For example, a life sciences company may want its chief research officer or chief medical officer on the internal team.

How does a reseller establish a reasonable belief that a person is a QIB?

The reseller (and any person acting on the reseller’s behalf) may rely on the following non-exclusive methods to establish a prospective purchaser’s ownership and discretionary investments in securities:

• The purchaser’s most recent publicly available annual financial statements; provided that such statements present the information as of a date within 16 months preceding the date of the sale of securities under Rule 144A to a U.S. purchaser, or within 18 months for a foreign purchaser;

• The most recent publicly available information filed by the prospective purchaser with (a) the SEC; another U.S. federal, state; or local governmental agency; or a self-regulatory organization, or (b) a foreign governmental agency or foreign self-regulatory organization; provided that such statements present the

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**Rule 144A Equity Offering Team**

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information as of a date within 16 months preceding the date of the sale of securities under Rule 144A to a U.S. purchaser, or within 18 months for a foreign purchaser;

• The most recent publicly available information appearing in a recognized securities manual, such as Moody’s or Standard & Poor’s; provided that such statements present the information as of a date within 16 months preceding the date of the sale of securities under Rule 144A to a U.S. purchaser, or within 18 months for a foreign purchaser; or

• A certification by the purchaser’s chief financial officer, a person fulfilling an equivalent function or other executive officer specifying the amount of securities owned and invested on a discretionary basis by the purchaser as of a specific date on or since the end of the purchaser’s most recent fiscal year or, in the case of a purchaser that is a member of a family of investment companies, a certification by an executive officer of the investment adviser specifying the amount of securities owned by the family of investment companies as of a specific date on or since the end of the purchaser’s most recent fiscal year.

The bases for reliance enumerated in Rule 144A are non-exclusive; resellers may be able to establish a reasonable belief of eligibility based on factors other than those cited.

A reseller cannot rely on certifications that it knows, or is reckless in not knowing, are false. However, a seller has no duty of verification. In other words, unless the circumstances give a reseller reason to question the veracity of the information, the reseller does not have a duty to verify the information.


How does a reseller typically satisfy the requirement of making a purchaser aware that the reseller may rely on Rule 144A in connection with the resale?

Typically, the warning is given by placing a legend on the security itself. For example, the stock certificate representing securities resold under Rule 144A will include a legend (or a notation for electronic records) stating that the securities have not been registered under the Securities Act and, therefore, may not be resold or otherwise disposed of in the absence of such registration or unless such transaction is exempt from, or not subject to, registration.

In addition, the offering memorandum or other offering document used in connection with the Rule 144A offering typically will include an appropriate notice to investors, such as the following:

“Each purchaser of the securities will be deemed to have represented and agreed that it is acquiring the securities for its own account or for an account with respect to which it exercises sole investment discretion, and that it or such account is a QIB and is aware that the sale is being made to it in reliance on Rule 144A.”

The offering memorandum or other offering document will also include a notice to purchasers that the securities to be acquired may only be reoffered and resold pursuant to an exemption from, or registration under, the Securities Act.

Finally, the securities will have a restricted CUSIP number.
What do the initial purchasers do?

The issuer will want to carefully identify one or more initial purchasers that will be responsible for the offering process. If the issuer wants to be in a position to complete an IPO soon after completion of the Rule 144A equity offering, the initial purchasers should be, or should include, registered broker-dealers that are qualified to serve as the underwriters of the proposed IPO. An initial purchaser may be chosen based on its industry expertise, including the knowledge and following of its research analysts, the breadth of its distribution capacity, and its overall reputation. As is the case with the underwriters of an IPO, the issuer should at a minimum consider the following questions:

- Does the investment bank have strong research in the issuer’s industry?
- Is the investment bank’s distribution network mainly institutional or retail?
- Is the investment bank’s strength domestic, or does it have foreign distribution capacity?

Depending on the offering size, an issuer may want to include a number of additional initial purchasers to complement the lead initial purchaser’s strengths and weaknesses.

As with an IPO, an issuer should keep in mind that the initial purchasers have at least two conflicting responsibilities—to resell the securities they purchase from the issuer and to recommend to potential purchasers that the purchase of the securities in a Rule 144A equity offering is a suitable and worthy investment. In order to learn about the issuer’s business—and to support a diligence defense for the initial purchasers in connection with the offering—the initial purchasers and their counsel should spend a substantial amount of time performing business, financial, and legal “due diligence” in connection with the Rule 144A equity offering, and making sure that the offering memorandum and any other offering materials are consistent with the information provided.

What do the auditors/accountants do?

If audited financial statements are provided by an issuer in connection with a Rule 144A equity offering, whether as part of an offering memorandum or to purchasers, the accountants will prepare and audit the financial statements. Even if the issuer determines not to include audited financial statements, the issuer will need to work closely with the auditors, and the auditors should review the financial statements and all other financial information to ensure that the issuer is applying appropriate accounting standards so that once the financial statements are audited there won’t be material changes from the reviewed financial information.

Other services that may be provided by accountants during the offering process include assisting the issuer in preparing the financial information to be included in the offering memorandum, such as the summary financial information, selected financial information, capitalization and dilution tables, and any pro forma financial statements; the accountants may also be asked to provide a “comfort letter” or an agreed-upon procedures letter to the initial purchasers. See “What are the disclosure requirements for Rule 144A equity offerings?” and more Frequently Asked Questions About Rule 144A—“What is a comfort letter?”

What does legal counsel do?

An issuer’s in-house and outside legal counsel play an important role in the Rule 144A equity offering process. Issuer’s counsel:
• Has principal responsibility for preparing any required offering documentation, including any post-offering registration statements covering the resale of the offered securities, if contemplated in the offering;
• Negotiates a purchase agreement with the initial purchasers and their counsel; and
• Prepares various other documents, including stock option plans, charter documents, committee charters, board minutes relating to the offering and any required consents, waivers, and legal opinions.

Counsel to the initial purchasers undertakes legal due diligence during the offering process and reviews and comments on the offering memorandum and other offering materials with the issuer, its counsel, and the initial purchasers. Counsel to the initial purchasers also:
• Negotiates the purchase agreement with the issuer and its counsel;
• Negotiates the “comfort letter,” if applicable; and
• Submits any required materials to the Financial Industry Regulatory Authority, Inc. (“FINRA”).

The issuer’s counsel and counsel to the initial purchasers will also coordinate the closing of the transaction.

What steps should be taken to prepare for a Rule 144A equity offering?

Issuers contemplating a Rule 144A equity offering should consider making many of the same legal and operational changes that issuers should make before proceeding with an IPO. Those issuers that are considering a Rule 144A equity offering at the same time they are considering an IPO will need to consider the changes. The changes should be effected well before any organizational meeting held to launch the offering. See “Frequently Asked Questions About Initial Public Offerings—What corporate steps should be taken to prepare for an IPO?”

What is the “due diligence” process?

The Rule 144A due diligence process is similar to that followed in connection with a registered public offering. Generally, the due diligence process is divided into two parts: (a) business and management due diligence, and (b) documentary, or legal, due diligence. In order to help establish their due diligence, the initial purchasers in a Rule 144A equity offering will request documents at closing similar to those delivered in an underwritten offering, including a comfort letter, legal opinions, and officer certificates.

A due diligence investigation is a critical component in an initial purchaser’s decision whether to undertake an offering, enabling the prospective purchaser to evaluate the relevant legal, business, and reputational risks. Rule 144A offerings do not subject the issuer and the initial purchasers to liability under Section 11 of the Securities Act. Nonetheless, a thorough due diligence investigation by lawyers, accountants, the issuer, and the initial purchasers necessarily produces better disclosure and mitigates liability or potential liability for material misstatements or omissions.

If the issuer is contemplating an IPO, either as an alternative to a Rule 144A equity offering or shortly after completion of the Rule 144A equity offering, the
underwriters of the proposed IPO may also serve as the initial purchasers in the equity 144A offering. In such case, switching between these formats will not necessarily involve a change in offering participants.

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**Offering Process**

*How are Rule 144A equity offerings structured?*

The Rule 144A offering process is similar to the public offering process. The features of this process typically include:

- Solicitation of orders using a preliminary offering memorandum;
- Preparation and delivery of a final term sheet to investors to indicate the final pricing terms;
- Confirmation of orders using a final offering memorandum;
- Execution of the purchase agreement at pricing;
- Delivery of the comfort letter at pricing;
- Delivery of legal opinions and other closing documents at closing; and
- Closing three to five days after pricing.

*What are the conditions that a reseller of the restricted securities must satisfy to rely on Rule 144A?*

There are four conditions to reliance on Rule 144A:

- Actual sales are made only to QIBs or to an offeree or purchaser that the reseller (and any person acting on its behalf) reasonably believes is a QIB (see “Frequently Asked Questions About Rule 144A—How does a reseller establish a reasonable belief that a person is a QIB?”);

- The reseller (or any person acting on its behalf) must take reasonable steps to ensure that the buyer is aware that the reseller may rely on Rule 144A in connection with the resale (see “Frequently Asked Questions About Rule 144A—How does a reseller typically satisfy the requirement of making a buyer aware that the reseller may rely on Rule 144A in connection with the resale?”);

- The securities reoffered or resold are eligible securities under Rule 144A (see “Frequently Asked Questions About Rule 144A—What securities are eligible for exemption under Rule 144A?”); and

- In the case of securities of an issuer that is neither an Exchange Act reporting company, nor a foreign issuer exempt from reporting pursuant to Rule 12g3-2(b) of the Exchange Act or a foreign government, the holder and a prospective buyer designated by the holder must have the right to obtain from the issuer and must receive, upon request, certain “reasonably current” information about the issuer.

Source: Rule 144A(d).

*What are road shows?*

Road shows or “dog and pony shows” are presentations where the issuer’s representatives (usually the CEO, CFO, and possibly an investor relations professional) and the initial purchasers meet with potential significant investors to discuss the issuer’s business and the offering. Attendance at a road show for a Rule 144A equity offering generally is limited to QIBs (or non-U.S. persons if the offering will be conducted in compliance
with Regulation S) although general solicitation is permitted in the context of the offering. If the issuer is a reporting company, the issuer will need to closely consider the content of a road show in light of Regulation FD. See “Frequently Asked Questions About Initial Public Offerings—What are road shows and what materials are permitted?”

**Can an issuer hold an electronic road show?**

Yes. Participation in electronic road shows, either through the Internet or otherwise, is usually limited to QIBs although general solicitation is permitted in the context of the offering. See “Frequently Asked Questions About Rule 144A—Can the Internet be used to make Rule 144A reoffers and resales?”

**May an issuer publicly announce its intention to complete a Rule 144A equity offering?**

Yes. Effective September 23, 2013, pursuant to Section 201 of the Jumpstart Our Business Startups (JOBS) Act, the SEC revised Rule 144A to permit general solicitation and general advertising of these offerings, provided actual sales are made only to persons that are reasonably believed to be QIBs. As a result, issuers and initial purchasers will have enhanced flexibility with respect to communications about Rule 144A offerings.

**Are the securities resold under Rule 144A freely tradable?**

No. Securities acquired in a Rule 144A transaction are deemed “restricted securities” within the meaning of Rule 144(a)(3) of the Securities Act. As a result, these securities remain restricted until the applicable holding period under Rule 144 expires and may only be publicly resold under Rule 144, pursuant to an effective registration statement, or in reliance on any other available exemption under the Securities Act. Exempt resales of restricted securities may be made in compliance with Rule 144A, the so-called Section 4(1½) exemption, or Regulation S. See “Frequently Asked Questions About Rule 144A—Why do Rule 144A purchasers often insist that the issuer register the securities issued in the Rule 144A transaction?”

Source: Preliminary Note No. 6 of Rule 144A.

**What are the holding periods applicable to the sale of Rule 144A securities?**

In December 2007, the SEC amended Rule 144 to, among other things, shorten the holding period for restricted securities (subject to certain public information requirements). For non-affiliate holders of restricted securities, Rule 144 provides a safe harbor for the resale of such securities without limitation after six months in the case of issuers that are reporting companies that comply with the current information requirements of Rule 144(c), and after one year in the case of non-reporting issuers. In each case, after a one-year holding period, resales of these securities by non-affiliates will no longer be subject to any other conditions under Rule 144.

For a reporting issuer, compliance with the adequate current public information condition requires the issuer to have filed all reports under Section 13 or Section 15(d) of the Exchange Act. For a non-reporting issuer, compliance with the adequate current public information condition requires making publicly available basic information about the issuer, including certain financial statements.

For affiliate holders of restricted securities, Rule 144 provides a safe harbor permitting resales of restricted securities, subject to the same six-month and one-year
holding periods for non-affiliates and to other resale conditions of amended Rule 144. These other resale conditions include, to the extent applicable: (a) adequate current public information about the issuer, (b) volume limitations, (c) manner of sale requirements for equity securities, and (d) notice filings on Form 144.

Source: Preliminary Note No. 2 of Rule 144. With respect to the resale of restricted securities pursuant to Rule 144, see J. William Hicks, *Resales of Restricted Securities*, at 5-1 (West Group 2007).

**How are Rule 144A securities registered under the Securities Act?**

The two principal methods to register the resale of Rule 144A eligible securities under the Securities Act are:

- “Exxon Capital” exchange offers; and
- Shelf registrations under Rule 415 of the Securities Act.

See also “Frequently Asked Questions About Rule 144A—What is an Exxon Capital exchange offering?”

**Can an issuer that is not an Exchange Act reporting company be required to register under the Exchange Act in connection with a Rule 144A equity offering?**

Yes. Section 12(g) of the Exchange Act requires any issuer (other than a bank or bank holding company) having 2,000 or more holders of record (or 500 non-accredited holders of record) of a class of equity securities and more than $10 million in assets at the end of its most recent fiscal year, anywhere in the world, to register the class of equity securities under the Exchange Act.

As a result, a non-reporting company that has sold equity securities in connection with a Rule 144A transaction may be required to register that class of equity securities. This may occur as a result of resales of the Rule 144A securities in the secondary market, other transactions that increase the number of holders, or, in the case of a foreign private issuer, a listing on NASDAQ. Issuers that effect “backdoor IPOs” under Rule 144A must be careful to monitor the number of their equity holders.

Source: Rule 12g3-2(a). Preliminary Note No. 4 of Rule 144A and SEC Release No. 33-6862 (April 23, 1990) state that Rule 144A does not affect the securities registration requirements of Section 12 of the Exchange Act.

**Is a Rule 144A security a “covered security” for purposes of Section 18 of the Securities Act?**

It depends. Section 18 of the Securities Act exempts certain securities and securities offerings from state regulation relating to registration and qualification of securities or securities transactions. However, states may continue to require notice filings to be made in connection with exempt securities or offerings.

Pursuant to Section 18, Rule 144A transactions are not subject to state regulation if (i) the issuer of the securities being resold in the Rule 144A transaction has a class of securities listed, or authorized for listing, on the New York Stock Exchange, NYSE MKT, or the NASDAQ, (ii) listed, or authorized for listing, on a national securities exchange that has listing standards that the SEC has determined by rule are substantially similar to the listing standards applicable to the securities described in clause (i), and (iii) the securities being resold in the Rule 144A transaction are equal or
senior to the issuer’s securities that are listed on one of the above-referenced markets. For example, if an issuer has senior debt securities traded on the New York Stock Exchange, and it offers common stock in a Rule 144A offering, the common stock will be “covered securities” under Section 18.

In addition, under Section 18, Rule 144A resales to “qualified purchasers” are exempt from state regulation. In December 2001, the SEC issued a proposed rule to define the term “qualified purchaser” for purposes of Section 18, but the proposed rule was never adopted. The proposed definition mirrors the definition of “accredited investor” under the Securities Act, but since the SEC never formally adopted the definition, most legal practitioners are reluctant to advise their clients that they may rely on it or, consequently, on this provision of Section 18.

If Section 18 does not exempt the Rule 144A transaction from state regulation, then the transaction will be required to be registered with each state in which the Rule 144A resales occur, or must otherwise be exempt from such state registration. Most state securities laws contain an exemption from registration for reoffers and resales made to QIBs within the meaning of Rule 144A. In states that do not have the specific exemption, Rule 144A sales are often exempt because Rule 144A purchasers would likely be deemed to be “institutional investors” for purposes of such states’ analogous institutional investor exemption.

Source: Preliminary Note No. 5 of Rule 144A and SEC Release No. 33-6862 (April 23, 1990) state that nothing in Rule 144A removes the need to comply with any applicable state law relating to the offer and sale of securities. See Section 18(b)(1)(C) with respect to the “qualified purchaser” exemption.

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FREQUENTLY ASKED QUESTIONS
ABOUT REGULATION S

Understanding Regulation S

What is Regulation S?

Regulation S provides an exclusion from the Section 5 registration requirements of the Securities Act of 1933, as amended (the “Securities Act”), for offerings made outside the United States by both U.S. and foreign issuers. A securities offering, whether private or public, made by an issuer outside of the United States in reliance on Regulation S need not be registered under the Securities Act. The Regulation S safe harbors are non-exclusive, meaning that an issuer that attempts to comply with Regulation S also may claim the availability of another applicable exemption from registration. Regulation S is available for offerings of both equity and debt securities.

Regulation S is available only for “offers and sales of securities outside the United States” made in good faith and not as a means of circumventing the registration provisions of the Securities Act. The availability of the issuer (Rule 903) and the resale (Rule 904) safe harbors is contingent on two general conditions:

- the offer or sale must be made in an offshore transaction; and
- no “directed selling efforts” may be made by the issuer, a distributor, any of their respective affiliates, or any person acting on their behalf.

Regulation S is composed of the following parts: eight preliminary notes; Rule 901, which contains a general statement of the regulation; Rule 902, which sets forth applicable definitions; Rules 903 and 904, which set forth the two safe harbors; and Rule 905, which sets forth the resale limitations applicable to equity securities.

Who may rely on Regulation S?

Members of the offering party, including:

- U.S. issuers – both reporting and non-reporting issuers may rely on the Rule 901 general statement or the Rule 903 issuer safe harbor;
- Foreign issuers – both reporting and non-reporting foreign issuers may rely on the Rule 901 general statement or the Rule 903 issuer safe harbor;
- Distributors (underwriters and broker-dealers) – both U.S. and foreign financial intermediaries may rely on the Rule 901 general statement or the Rule 903 issuer safe harbor;
- Affiliates of the issuer – both U.S. and foreign;
• Any persons acting on the behalf of the aforementioned persons;
• Non-U.S. resident purchasers (including dealers) who are not offering participants may rely on the Rule 901 general statement or the Rule 904 resale safe harbor to transfer securities purchased in a Regulation S offering; and
• U.S. residents (including dealers) who are not offering participants may rely on the Rule 901 general statement or the Rule 904 resale safe harbors in connection with purchases of securities on the trading floor of an established foreign securities exchange that is located outside the United States or through the facilities of a designated offshore securities market.

Who may not rely on Regulation S?
Regulation S is not available for the offer and sale of securities issued by open-end investment companies, unit investment trusts registered or required to be registered under the Investment Company Act of 1940 (the “1940 Act”), or closed-end investment companies required to be registered, but not registered, under the 1940 Act.

What types of transactions are conducted under Regulation S?
There are several types of Regulation S offerings that U.S. or foreign issuers may conduct:
• a standalone Regulation S offering, in which the issuer conducts an offering of debt or equity securities solely in one or more non-U.S. countries;
• a combined Regulation S offering outside the United States and Rule 144A offering inside the United States; and
• Regulation S continuous offering programs for debt securities, including various types of medium-term note programs (these continuous offering programs may be combined with an issuance of securities to qualified institutional buyers (“QIBs”) in the United States under Rule 144A).

Two other types of offerings also are permitted by Regulation S: (1) offerings made under specified conditions pursuant to an employee benefit plan established and administered in accordance with law of the country other than United States and in accordance with that country’s practices and documentation; and (2) offerings of foreign government securities.

The Regulation S portion of any offering refers only to the portion of the offering that requires the offering participants to comply with Regulation S in order to benefit from the safe harbor. The offering itself also must comply with the requirements of the applicable non-U.S. jurisdictions and the requirements of any foreign securities exchange or other listing authority. A Regulation S-compliant offering could be combined with a registered public offering in the United States or an offering exempt from registration in the United States, as well as be structured as a public or private offering in one or more non-U.S. jurisdictions.

What conditions must be satisfied to rely on Regulation S?
Both the issuer and resale safe harbors of Regulation S are available to market participants only if (1) the offer or sale is made as part of an “offshore transaction” and
(2) none of the parties make any “directed selling efforts” in the United States. In addition, offerings made in reliance on Rule 903 are subject to additional restrictions that are calibrated to the level of risk that securities in a particular type of transaction will flow back into the United States.

Rule 903 distinguishes three categories of transactions based on the type of securities being offered and sold, whether the issuer is domestic or foreign, whether the issuer is a reporting issuer under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and whether there is a “substantial U.S. market interest” or “SUSMI.”

“Category 1” transactions are those in which the securities are least likely to flow back into the United States. Therefore, the only restrictions are that the transaction must be an “offshore transaction” and that there be no “directed selling efforts” in the United States.

“Category 2” and “Category 3” transactions are subject to an increasing number of offering and transactional restrictions for the duration of the applicable “distribution compliance period.” “Distribution compliance period” is defined in Rule 902(f) generally as the period following the offering when any offer or sales of Category 2 or 3 securities must be made in compliance with the requirements of Regulation S in order to prevent the flow back of the offered securities into the United States. The period ranges from 40 days to six months for reporting issuers or one year for equity securities of non-reporting issuers.

For further discussion of transactions conducted under Categories 1, 2 and 3, see “Eligible Transactions” below.

Can issuers conduct exempt or excluded offerings concurrently with Regulation S transactions?

Yes. For purposes of determining whether Rule 903’s general requirement for offshore transactions is met, a contemporaneous registered offering or exempt private placement in the United States will not be integrated with an offshore offering that otherwise complies with Regulation S. In fact, Regulation S contemplates that a private placement in the United States may be made simultaneously with an offshore public offering in reliance on the issuer safe harbor. Thus, offshore offerings and sales of securities made in reliance on Regulation S do not preclude the resale of those same securities made in reliance on Rule 144A or Regulation D, even if the resale occurs during the distribution compliance period. Conversely, in determining whether the requirements for a Section 4(a)(2) exempt private placement are met, offshore transactions made in compliance with Regulation S will not be integrated with domestic offerings that are otherwise exempt from registration under the Securities Act.

What are the holding periods applicable to the sale of Regulation S securities?

Securities cannot be offered or sold to a U.S. person during the distribution compliance period unless the transaction is registered under the Securities Act or exempt from registration. There is no distribution compliance period in connection with securities sold in a Category 1 transaction. The distribution compliance period for Category 2 transactions involving both equity and debt securities and for Category 3 transactions involving debt securities is 40 days. The distribution compliance period for Category 3 offerings of equity securities is six months, if the issuer is a reporting
company, and one year otherwise. The difference in the length of the distribution compliance period for reporting issuers and non-reporting issuers was implemented by the Securities and Exchange Commission (the “SEC”) in 2008 in connection with amendments to Rules 144 and 145 of the Securities Act. Prior to these amendments, all Category 3 equity securities were subject to a one-year distribution compliance period.

Under Rule 902(f), the distribution compliance period begins on the later of (1) the date when the securities were first offered to persons other than distributors, or (2) the date of the closing of the offering, and continues until the end of the time period specified in the relevant provision of Rule 903. All offers and sales by a distributor of an unsold allotment are considered to be made during the distribution compliance period.

**How is the distribution compliance period measured for different types of securities?**

Distribution compliance periods for continuous offerings of medium-term notes, warrants, convertible securities, and American depositary receipts (“ADRs”) are measured differently:

1. **Medium-Term Notes.**

   In the case of continuous offerings, the distribution compliance period is deemed to begin at the completion of the distribution, as determined and certified by the managing underwriter or person performing similar functions. For continuous offering programs, such as medium-term note programs, the distribution compliance period is determined on a tranche-by-tranche basis. As to any tranche, the distribution compliance period begins when the manager for the offering certifies the completion of the distribution of that tranche.

2. **Warrants.**

   Securities underlying warrants are considered to be subject to a continuous distribution as long as the warrants remain outstanding, provided that the legending and certification requirements of Rule 903(b)(5), which are designed to limit the exercise of warrants by U.S. persons, are satisfied. The distribution compliance period will commence upon completion of the distribution of the warrants, as determined and certified by the managing underwriter or person performing similar functions.

3. **Convertible Securities.**

   In the case of convertible securities, both the convertible security and the underlying security are treated in the same manner. The distribution compliance period for both the convertible and the underlying security typically commences on the later of: (1) the date on which the offering of the convertible security closes, or (2) the date on which the convertible security was first offered to persons other than distributors in reliance on Regulation S. If, however, conversion of the convertible security is not exempt under section 3(a)(9) of the Securities Act, the convertible security will be treated in the same manner as a warrant.

4. **ADRs.**

   ADRs are issued by U.S. depositary banks and each represents one or more shares, or a fraction of a share, of a foreign issuer. ADRs allow foreign equity securities to be traded on U.S. stock exchanges. Ownership of an ADR entitles one to the right to obtain the foreign share that the ADR represents, although most U.S. investors
find it is easier to own just the ADR. An American depositary share (“ADS”), on the other hand, is the actual underlying foreign share that an ADR represents. The issuance of ADRs in exchange for the underlying foreign shares or the withdrawal of deposited ADRs during the distribution compliance period is not precluded by Regulation S.

Does Regulation S apply to resales of equity securities?
Yes. Under Rule 905, equity securities acquired from the issuer, a distributor or their respective affiliates in a transaction subject to the conditions of Rules 901 or 903 are deemed to be restricted securities as defined in Rule 144 under the Securities Act (there is no similar rule for debt securities). Therefore, an offshore purchaser can resell such securities only in accordance with Regulation S (in which case a distribution compliance period may apply) or the registration requirements of the Securities Act. Any restricted securities or equity securities of a domestic issuer will continue to be restricted securities despite the fact that such securities were acquired in a resale transaction pursuant to Rules 901 or 904. However, Rule 905 only applies to equity securities that, at the time of issuance, were those of a domestic issuer.

Eligible Transactions

What types of transactions are eligible for exclusion under Regulation S?

1. **Category 1 Transactions.**

   Category 1 transactions include offerings of:
   - securities by foreign issuers who reasonably believe at the commencement of the offering that there is no SUSMI in certain securities;
   - securities by either a “foreign issuer” or, in the case of non-convertible debt securities, a U.S. issuer, in an “overseas directed offering”;
   - securities backed by the full faith and credit of a foreign government or sovereign, including securities issued directly by a foreign government or sovereign or a political subdivision thereof and securities guaranteed by a foreign government or sovereign or political subdivision thereof; and
   - securities by foreign issuers pursuant to an employee benefit plan established under foreign law.

Since Category 1 securities are deemed the least likely to flow back into the U.S., there are no additional precautionary limitations imposed in connection with Category 1 transactions by foreign issuers. For Category 1 transactions, there is no distribution compliance period during which time the securities may not be resold. However, issuers engaging in a Category 1 transaction that includes a Rule 144A tranche may choose to impose a 40-day distribution compliance period.

Under Rules 902(e) and 405, a “foreign issuer” refers to any issuer which is “a foreign government, a national of any foreign country or a corporation or other organization incorporated or organized under the laws of any foreign country”; and under Rule 903, an “overseas directed offering” refers to the offering of

1 Foreign governments or sovereigns or political subdivisions thereof also frequently register securities under Schedule B of the Securities Act. Schedule B offers a separate and generally more streamlined registration process for sovereign issuers compared with the process for domestic issuers and foreign private issuers, which are not entitled to use Schedule B. Schedule B requires a short list of disclosures compared with registration statements for other registered securities offerings.
securities of a foreign issuer directed into a single
country other than the United States in accordance with
that country’s local laws and customary practices.

2. **Category 2 Transactions.**

Category 2 transactions include offerings of:

- equity securities of a reporting foreign issuer;
- debt securities of a reporting U.S. or foreign
  issuer; and
- debt securities of a non-reporting foreign
  issuer.

The Category 2 safe harbor is available even if there is
a substantial U.S. market interest in the securities. All
Category 2 securities are subject to a 40-day distribution
compliance period. For purposes of Category 2, debt
securities include non-participating preferred stock and
asset-backed securities.

3. **Category 3 Transactions**

Category 3 is the residual safe harbor because it
applies to all transactions not eligible for the Category 1
or Category 2 safe harbors. Category 3 transactions
include:

- debt or equity offerings by non-reporting U.S.
  issuers;
- equity offerings by U.S. reporting issuers; and
- equity offerings by non-reporting foreign
  issuers for which there is a substantial U.S.
  market interest.

The risk of flow back into the United States is highest
for these securities. Consequently, Category 3 has the
most restrictions, and requires a six-month distribution
compliance period for equity securities of reporting
issuers and a one-year period for equity securities of
non-reporting issuers. For purposes of Category 3, debt
offerings include offerings of non-participating
preferred stock and asset-backed securities.

**What is an “offshore transaction”?

**

Rule 902(h) provides that any offer, sale, and resale is
part of an “offshore transaction” if:

- no offer is made to a person in the United
  States; and
- either (1) at the time the buy order is
  originated, the buyer is (or is reasonably
  believed to be by the seller) physically outside
  the United States, or (2) the transaction is for
  purposes of Rule 903, executed on a physical
  trading floor of an established foreign
  securities exchange, or for purposes of Rule
  904, executed on a “designated offshore
  securities market” and the seller is not aware
  that the transaction has been pre-arranged with
  a U.S. purchaser.

A buyer is generally deemed to be outside the United
States if the buyer (as opposed to the buyer’s agent) is
physically located outside the United States. However,
if the buyer is a corporation or investment company, the
buyer is deemed to be outside the United States when
an authorized agent places the buy order while
physically situated outside the United States.

Notwithstanding Rule 902(h)(1), offers and sales of
securities specifically directed at identifiable groups of
U.S. citizens abroad, such as members of the U.S. armed
forces serving overseas, are not considered to be
offshore transactions. In addition, offers and sales of
securities made to persons excluded from the definition
of “U.S. person,” even if physically present in the
United States, are deemed to be made in offshore
transactions.
Under Rule 902(b), “designated offshore securities market” refers to (1) various foreign securities exchanges, including, but not limited to, the London Stock Exchange, the Bourse de Luxembourg, the Tokyo Stock Exchange, and the Toronto Stock Exchange, and (2) any foreign securities exchange or non-exchange market designated by the SEC. Factors that the SEC may consider in determining whether to designate an offshore securities market include, among others:

- organization under foreign law;
- association with a generally recognized community of brokers, dealers, banks, or other professional intermediaries with an established operating history;
- oversight by a governmental or self-regulatory body;
- oversight standards set by an existing body of law;
- reporting of securities transactions on a regular basis to a governmental or self-regulatory body;
- a system for exchange of price quotations through common communications media; and
- an organized clearance and settlement system.

What are “directed selling efforts”?

The Rule 903 issuer safe harbor is only available to issuers, distributors, affiliates and any persons acting on their behalf if they make no directed selling efforts within the United States or to U.S. persons. “Directed selling efforts” is defined by Rule 902(c) as “any activity undertaken for the purpose of, or that could be reasonably expected to result in, conditioning the U.S. market for the relevant securities.” This applies during the offering period as well as during the distribution compliance period. Violation of the prohibition against directed selling efforts by any of these parties precludes reliance on the safe harbor. However, selling efforts could still be initiated from the United States, provided that these efforts are directed or effected abroad.

The following activities constitute “directed selling efforts” targeted at U.S. persons:

- advertising the offering in publications with a “general circulation” in the United States (which includes any publication printed primarily for distribution in the United States or that has had on average a circulation of at least 15,000 copies per issue within the prior twelve months);
- mailing printed materials to U.S. investors;
- conducting promotional seminars in the United States;
- placing advertisements with radio or television stations that broadcast in the United States; and
- making offers directed at identifiable groups of U.S. citizens in a foreign country, such as members of the U.S. military.

Rule 902 specifically excludes certain advertisements and activities from the definition of “directed selling efforts,” including the following:

- an advertisement required to be published by U.S. or foreign laws, regulatory or self-regulatory authorities, where the advertisement contains no more information than that which is legally required and includes a legend disclosing that the securities have not been registered under the Securities
Act and may not be offered or sold in the United States (or to a U.S. person, if the advertisement relates to a Category 2 or 3 offering) absent registration or reliance on an applicable exemption from the registration requirements of the Securities Act;

- a communication with persons excluded from the Rule 902(k) definition of U.S. person;

- a tombstone advertisement in a publication having less than 20% of its worldwide circulation in the United States that contains the following:
  
  - a legend disclosing that the securities have not been registered under the Securities Act, and may not be offered or sold in the United States (or to a U.S. person, if the advertisement relates to a Category 2 or 3 offering) absent registration or an applicable exemption from registration; and

  - limited permitted information, including: (1) the issuer’s name and a brief indication of its business; (2) the amount, title, and price of the securities sold; (3) the yield of any debt securities with a fixed interest rate; (4) the name and address of the managing underwriters; (5) the dates on which sales commence and conclude; and (6) whether the securities are or were offered by rights issued to security holders, and if so, the class of securities entitled to subscribe, the subscription ratio, record date, any dates upon which the rights were issued and expired, and the subscription price.

- bona fide visits and tours of real estate facilities in the United States by prospective investors;

- quotations of a foreign broker-dealer distributed by a third party system that primarily distributes this information in foreign countries, provided that no security transaction can be executed through the system between broker-dealers and persons in the United States, and no communication with U.S. persons is initiated;

- a notice in accordance with Rule 135 or 135c of the Securities Act that an issuer intends to make a registered or unregistered offering of its securities (which is similar to the permitted tombstone advertisement discussed above, and contains a legend and limited information about the issuer and the offering);

- providing journalists with access to issuer meetings held outside the United States, or providing written press or press-related materials released outside the United States in compliance with Rule 135e of the Securities Act;

- isolated limited contact within the United States;

- routine activities conducted in the United States unrelated to selling efforts, including normal communications to shareholders; and
• publication and distribution of research reports by a broker or dealer under Rule 138(c) or 139(b) of the Securities Act.²

Because of the fine line demarcating “directed selling efforts” from legitimate offering activities in certain contexts, further discussion is warranted for Internet postings, foreign press-related activity, research reports released by broker-dealers, offering notices, and advertising.

What is a “U.S. person”?

Pursuant to Rule 902(k)(1), the following are “U.S. persons”:

• any natural person resident in the United States;
• any partnership or corporation organized or incorporated under the laws of the United States;
• any estate of which any executor or administrator is a U.S. person;
• any trust of which any trustee is a U.S. person;
• any agency or branch of a U.S. person located outside the United States;
• any non-discretionary or similar account (other than an estate or trust) held by a dealer or other fiduciary for the benefit or account of a U.S. person;
• any discretionary or similar account (other than an estate or trust) held by a dealer or other fiduciary organized, incorporated or, if an individual, resident in the United States; and
• any partnership or corporation if (1) organized or incorporated under the laws of any foreign jurisdiction, and (2) formed by a U.S. person principally for the purpose of investing in securities not registered under the Securities Act, unless it is organized or incorporated and owned by accredited investors under Rule 501(a) of the Securities Act who are not natural persons, estates, or trusts.

Rule 902(k)(2) explicitly excludes the following from the definition of “U.S. person”:

• any discretionary or similar account (other than an estate or trust) held for the benefit or account of a non-U.S. person by a dealer or other professional fiduciary organized, incorporated or, if an individual, resident in the United States;
• any estate of which any professional fiduciary acting as executor or administrator is a U.S. person, if (1) an executor or administrator who is not a U.S. person has sole or shared investment discretion with respect to the assets of the estate, and (2) the estate is governed by foreign law;
• any trust of which any professional fiduciary acting as trustee is a U.S. person, if a trustee who is not a U.S. person has sole or shared investment discretion with respect to the trust assets, and no beneficiary of the trust (and no settler if the trust is revocable) is a U.S. person;
• an employee benefit plan established and administered in accordance with the laws, etc.

² Rules 138(c) and 139(b) of the Securities Act apply to Exchange Act reporting companies and foreign private issuers, but not foreign governments or sovereigns or political subdivisions thereof.
customary practices, and documentation of a country other than the United States;
• any agency or branch of a U.S. person located outside the United States if (1) the agency or branch operates for valid business reasons; and (2) the agency or branch is engaged in the business of insurance or banking, and is subject to substantive insurance or banking regulation in the jurisdiction where it is located; and
• such international organizations (and their agencies, affiliates and pension plans) as the International Monetary Fund, the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, and the United Nations.

In addition, contacts with certain of the non-U.S. persons listed above, even if made within the United States, are still not considered to be “directed selling efforts.”

Information Requirements

What reasonable steps must the reseller take to make the buyer aware that the reseller may rely on Regulation S in connection with the resale?

1. Offering Memorandum.

   If the offering is a standalone Regulation S offering (or a Regulation S tranche of a combined Rule 144A/Regulation S offering), and the securities are either Category 2 or Category 3, the offering memorandum (which is similar to a prospectus) and any other offering materials and documents (other than press releases) used in connection with offers and sales prior to the expiration of the applicable distribution compliance period must include:

   • statements to the effect that the securities have not been registered under the Securities Act and may not be offered or sold in the United States or to U.S. persons (other than distributors) unless the securities are registered under the Securities Act, or an exemption from such registration requirements is available; and
   • for equity securities of domestic issuers, an additional statement that hedging transactions involving those securities may not be conducted unless in compliance with the Securities Act.

In addition, for Category 3 equity securities:

   • the offer or sale, if made prior to the expiration of the one-year distribution compliance period (six months for a reporting issuer), may not be made to a U.S. person or for the account or benefit of a U.S. person (other than a distributor); and
   • the offer or sale, if made prior to the expiration of the applicable one-year or six-month distribution compliance period, is made pursuant to the following conditions:
     • the purchaser (other than a distributor) certifies that it is not a U.S. person and is not acquiring the securities for the account or benefit of any U.S. person or is a U.S. person who purchased securities in a transaction that did not require registration under the Securities Act; and
     • the purchaser agrees to resell such securities only in accordance with the provisions of
Regulation S, pursuant to registration under the Securities Act, or pursuant to an available exemption from registration; and agrees not to engage in hedging transactions with regard to such securities unless in compliance with the Securities Act.

The purchaser’s certifications are set forth in the offering memorandum and in most cases, a purchaser is deemed to have made such representations when it purchases beneficial interests in the Regulation S global security.

The offering memorandum for a combined Rule 144A/Regulation S offering contains extensive disclosure regarding resale limitations and transfer restrictions. If the securities will be held in book-entry format, as is customary, the disclosure also will include information regarding:

- the book-entry process and the forms of global securities;
- the delivery of the securities;
- the depositary procedures of DTC, Euroclear and Clearstream as holders of the book-entry certificates, particularly with respect to payments and any voting rights relating to the securities;
- the exchange of global notes for certificated notes, which is required under specified circumstances, and generally the prohibition on the exchange of certificated notes for beneficial interests in the global notes;
- exchanges between the Rule 144A security and any Regulation S security;
- same day settlement and payment procedures; and
- any registration rights, including discussion of any registered exchange offer.

2. Legend.

Regulation S requires that the certificates for the securities of a domestic issuer contain a legend to the effect that transfer is prohibited except in accordance with the provisions of Regulation S, pursuant to registration under the Securities Act, or pursuant to an available exemption from registration; and that hedging transactions involving those securities may not be conducted unless in compliance with the Securities Act. A sample Rule 903 legend would read: “These securities will be offered only outside of the United States to non-U.S. persons, pursuant to the provisions of Regulation S of the U.S. Securities Act of 1933, as amended. These securities will not be registered under the Securities Act, and may not be offered or sold in the United States absent registration or an applicable exemption from the registration requirements.”

The issuer of a Regulation S security also is required, either by contract or a provision in its bylaws, articles, charter or comparable document, to refuse to register any transfer of the securities not made in accordance with the provisions of Regulation S, pursuant to registration under the Securities Act, or pursuant to an available exemption from registration. However, the SEC recognized that securities of foreign issuers are often issued in bearer form and that foreign law may prevent the issuer for refusing to register securities transfers. Therefore, in such cases, Regulation S permits an issuer to implement “other reasonable procedures” (such as the legends described above) to prevent any transfer of the securities not made in accordance with the provisions of Regulation S.
3. **Confirmation**

Regulation S also requires each distributor selling securities to a distributor, a dealer, or a person receiving a selling concession, fee or other remuneration, prior to the expiration of a 40-day distribution compliance period in the case of debt securities, or the applicable one-year or six-month distribution compliance period in the case of equity securities, to send a confirmation or other notice to the purchaser stating that the purchaser is subject to the same restrictions on offers and sales that apply to a distributor.

**Conducting Regulation S Transactions**

**How are Regulation S transactions structured?**

1. **Debt Securities**

   **(A) Category 1 Safe Harbor**

   The issuer safe harbor is available for debt offerings if a foreign issuer reasonably believes at the commencement of the offering that there is no SUSMI in the debt securities. A SUSMI in debt securities exists if:

   - the issuer’s debt securities are held of record by 300 or more U.S. persons, and
   - U.S. persons hold of record at least 20% and at least $1 billion or more of the principal amount of debt securities, plus the greater of the liquidation preference or par value of non-participating preferred stock, and the principal amount or balance of asset-backed securities.

   If there is no SUSMI in a foreign issuer’s debt securities, the issuer need only comply with the general Regulation S requirements (i.e., offshore transaction and no directed selling efforts).

   Alternatively, foreign issuers of debt securities (and U.S. issuers of non-convertible debt securities) may rely on the Category 1 safe harbor if the transaction qualifies as an overseas directed offering. An offering of non-convertible debt securities of a U.S. issuer must similarly be directed into a foreign country in accordance with that country’s local laws and customary practices, and the securities must be non-U.S. dollar denominated or linked securities in order to qualify as an overseas directed offering. In addition, foreign issuers offering debt securities backed by the full faith and credit of a foreign government or that are offered pursuant to an employee benefit plan may rely on the Category 1 safe harbor, provided that the offers and sales are made as part of an offshore transaction and no directed selling efforts are made.

   **(B) Category 2 Safe Harbor**

   The issuer safe harbor is available to foreign issuers (both reporting and non-reporting) and reporting U.S. issuers of debt securities, subject to compliance with the offering and transactional restrictions for the applicable distribution compliance period.

   The following offering restrictions must be observed by the issuer, as well as by its affiliates and any distribution participants:

   - each distributor must agree in writing to the following:
     - all offers and sales of the securities prior to the expiration of a forty-day distribution compliance period must be made in accordance with Rule 903, pursuant to registration under the...
Securities Act or to an exemption from registration; and

- for any offers and sales of equity securities of U.S. issuers, not to engage in hedging transactions with respect to such securities prior to the expiration of the distribution compliance period, unless in compliance with the Securities Act;

- all offering materials and documents (except press releases) used in connection with offers and sales of the securities prior to the expiration of the distribution compliance period must include legends in specified places in the prospectus or offering circular and in advertisements disclosing that the securities have not been registered under the Securities Act and may not be offered or sold in the United States or to U.S. persons (except distributors) absent registration under the Securities Act or in reliance on an exemption from registration; and

- the offering materials and documents relating to equity securities of U.S. issuers must state that hedging transactions involving such securities may not be conducted unless in compliance with the Securities Act.

An issuer must also comply with the following transactional restrictions:

- no offer or sale is made during the distribution compliance period to (or for the account or benefit of) a U.S. person, except for distributors; and

- each distributor selling securities to a distributor, a dealer, or a person receiving a selling concession, fee or other remuneration with respect to the securities sold, prior to the expiration of the distribution compliance period, sends a confirmation or other notice to the purchaser stating that the purchaser is subject to the same restrictions on offers and sales.

Non-compliance with the offering restrictions renders the safe harbor unavailable to all distribution participants. By contrast, noncompliance with the transactional restrictions renders the safe harbor unavailable only for the party (and its affiliates and persons acting on their behalf) that failed to comply with the restrictions.

(C) Category 3 Safe Harbor

The issuer safe harbor is available to non-reporting U.S. issuers of debt securities, provided that the debt securities are not offered or sold to (or for the benefit of) a U.S. person (other than a distributor) during the 40-day distribution compliance period, except pursuant to the registration requirements of the Securities Act or an exemption from registration. Issuers must comply with the offering and transactional restrictions applicable to Category 2 offerings and Rule 903(b)(3)’s three additional transactional restrictions during the distribution compliance period:

- the securities may not be offered or sold to (or for the account or benefit of) a U.S. person other than a distributor;

- the securities must be represented by a temporary global security that cannot be
exchanged for definitive securities (1) by distributors until the end of the distribution compliance period; and (2) for persons other than distributors, until certification of beneficial ownership of the securities by non-U.S. persons (or by any U.S. person who purchased the securities in an exempt transaction); and

- any distributor selling securities to another distributor or to a dealer or any person receiving a selling concession or similar compensation must send confirmation to the purchaser before the end of the distribution compliance period stating that the purchaser is subject to the same restrictions on offers and sales applicable to a distributor.

2. **Equity Securities**

   Regulation S uses the definition of “equity security” set forth in Rule 405 of the Securities Act. Under Rule 405, “equity security” refers to:

   - any stock or similar security, certificate of interest or participation in any profit sharing agreement, pre-organization certificate or subscription, transferable share, voting trust certificate or certificate of deposit for an equity security, limited partnership interest, interest in a joint venture, or certificate of interest in a business trust;
   - any security future on any such security;
   - any security convertible, with or without consideration into such a security, or carrying any warrant or right to subscribe to or purchase such a security;
   - any such warrant or right; or
   - any put, call, straddle, or other option or privilege of buying such a security from or selling such a security to another without being bound to do so.

The provisions of the issuer safe harbor that are specific to offerings of equity securities are summarized below.

(A) **Category 1 Safe Harbor**

   The Category 1 safe harbor is available for equity offerings if a foreign issuer reasonably believes at the beginning of the offering that there is no SUSMI in the equity securities. A SUSMI in equity securities exists if, during the shorter of the issuer’s prior fiscal year or the period since incorporation, either:

   - the U.S. securities exchanges and inter-dealer quotation systems in the aggregate, constituted the single largest market for a class of the issuer’s securities; or
   - at least 20% of all trading in a class of the issuer’s securities occurred on the facilities of U.S. securities exchanges and inter-dealer quotation systems, and less than 55% of such trading occurred on the facilities of the securities markets of a single foreign country.

   If there is no SUSMI in a foreign issuer’s equity securities, the issuer need only comply with the general Regulation S requirements to make offers and sales.

(B) **Category 2 Safe Harbor**

   The Category 2 safe harbor is only available for equity offerings by a reporting foreign issuer. Even if there is a SUSMI in the securities, reporting foreign issuers who implement the Category 2 offering and
transactional restrictions for the distribution compliance period may rely on the safe harbor.

(C) Category 3 Safe Harbor

The Category 3 safe harbor is available to any issuer of equity securities who, for the duration of a distribution compliance period of one year (or six months, if the issuer is a reporting company), implements and complies with the Category 2 offering and transactional restrictions and the following additional restrictions:

- the purchaser of the securities (except a distributor) must either certify (1) that it is not a U.S. person and is not acquiring the securities for the account or benefit of any U.S. person; or (2) that it is a U.S. person who purchased securities in a transaction under an applicable exemption from registration under the Securities Act;

- the purchaser of the securities must agree to resell the securities only in accordance with Regulation S, pursuant to the registration requirements of the Securities Act or in reliance on an exemption from registration;

- the purchaser of the securities must agree not to engage in hedging transactions unless in compliance with the Securities Act;

- the securities of a U.S. issuer must contain a legend stating that (1) the transfer of the securities is prohibited unless made in accordance with Regulation S, pursuant to the registration requirements of the Securities Act or in reliance on an exemption from registration; and (2) hedging transactions involving those securities must be made only in compliance with the Securities Act;

- the issuer must be required by contract or by its charter, bylaws or similar document to refuse to register any transfer made in violation of Regulation S unless the securities are in bearer form or foreign law prevents the issuer from refusing to register transfers. In the latter two instances, the issuer must implement other reasonable procedures in order to prevent any transfer of securities not made in accordance with Regulation S. For example, an issuer may include a legend on the securities stating that transfers not made in accordance with Regulation S, the registration requirements of the Securities Act or in reliance on an exemption from registration, are prohibited; and

- any distributor selling securities to another distributor or to a dealer or any person receiving a selling concession or similar compensation must send confirmation to the purchaser before the end of the distribution compliance period stating that the purchaser is subject to the same restrictions on offers and sales applicable to a distributor.

What type of documentation is typically involved in a Regulation S offering of debt securities?

Regulation S offerings are typically combined with Rule 144A offerings. The documentation typically used in both debt and equity Rule 144A transactions, with or without a Regulation S tranche, is similar to that used in
registered offerings, including:

- an offering memorandum, which is similar to a prospectus;
- a purchase agreement between the issuer and the initial purchasers, which is similar to an underwriting agreement;
- an agreement among underwriters or syndication agreement;
- in some cases, a registration rights agreement between the issuer and the initial purchasers;
- in a debt offering, an indenture;
- comfort letters from the issuer’s auditors; and
- closing documentation including “bring down” comfort letters, legal opinions, a “10b-5” or “negative assurance” letter from legal counsel, and closing certificates.

As in a public registered offering, the issuer will work with its counsel, investment bank, investment bank’s counsel and independent accountants to prepare the necessary documents.

In the case of a Rule 144A offering that is combined with a Regulation S offering, the Regulation S offering may be conducted using documents that are based on the country-specific practices of the relevant non-U.S. jurisdiction or jurisdictions. However, the disclosure documents in such a case generally will contain the same substantive information so that investors have the same “disclosure package.”

U.S. issuers commonly use U.S. style underwriting documents in offerings targeted at U.S. investors. However, offerings by non-U.S. issuers or led by non-U.S. financial intermediaries may use underwriting documentation that follows local practices, particularly if the Rule 144A tranche is small.

3. Offering Memorandum.

Regardless of the type of issuer, if the Regulation S tranche is an offering of Category 2 or Category 3 securities, all participants (including the issuer and its affiliates and persons acting on behalf of either) are responsible for ensuring that all offering materials and documents other than press releases used in connection with the offer or sale of securities during the distribution compliance period bear legends stating that the securities have not been registered under the Securities Act and may not be offered or sold in the United States or to a U.S. person, absent registration under the Securities Act or in reliance on an exemption therefrom. Moreover, in the case of equity securities offered by U.S. issuers, the legends must also state that hedging transactions may not be conducted except in compliance with the Securities Act. These legends must appear both on (or inside) the cover page and in the underwriting section of any offering memorandum used in connection with the offer or sale of securities (if the legend is on the front page of the offering memorandum, it may be printed in summary form). The legends must also be printed in any advertisement made or issued by the issuer, any distributor, and their respective affiliates or representatives. In addition, because of the complexity of clearance and settlement

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3 Many broker-dealers are already party to a “master agreement among underwriters” that governs the relationship among syndicate members. Therefore, a deal-specific agreement among underwriters typically is not required. Combined offerings that are syndicated to a substantial number of non-U.S. broker-dealers may use a number of syndication agreements, including agreements among underwriters (on a per syndicate level), intersyndicate agreements and transaction-specific dealer agreements. The International Primary Market Association’s Standard Form Agreement Among Managers is sometimes used in Regulation S debt offerings syndicated primarily to London-based broker-dealers.
procedures in global offerings, an offering memorandum usually includes extensive clearance and settlement discussions.

Once the preliminary offering memorandum is prepared, unlike a public offering, it is not subject to SEC review and the only subsequent changes are to disclose changes in the issuer’s business, financial condition or other circumstances and to provide the final terms of the securities and the offering.

4. Purchase Agreement

In a combined Rule 144A/Regulation S transaction, a purchase agreement will contain standard representations and warranties related to the issuer, the securities offered, the business and other representations designed to supplement the due diligence investigation of the initial purchasers. In addition, the agreement will contain representations, warranties and covenants specific to the Rule 144A/Regulation S offering, including:

- the issuer will not use “directed selling efforts” as defined under Regulation S, and if the securities offered are Category 2 or 3 securities, it has implemented the necessary Regulation S offering restrictions;
- the issuer has not engaged in general solicitation or general advertising (unless the issuer chooses to use general solicitation or general advertising, which are now permitted for Rule 144A offerings so long as the securities are sold to a QIB or to a purchaser that the seller and any person acting on the seller’s behalf reasonably believes is a QIB);
- the offered securities meet the eligibility requirements under Rule 144A;
- the issuer is not an open-end investment company, unit investment trust or face-amount certificate company; and
- if the securities are debt securities or ADRs, the issuer will not resell any securities in which it or any of its affiliates has acquired a beneficial ownership interest.

In addition, if the offering involves common equity, either directly or upon conversion of preferred stock or debt securities or upon exercise of warrants, the initial purchaser may require the issuer and even its senior management or other shareholders to “lock up” their common stock.

Unlike an underwriting agreement for a public offering, the initial purchasers in a combined Rule 144A/Regulation S transaction will also make limited representations, warranties and covenants. The initial purchasers, as “distributors” (within the meaning of Regulation S) will also represent, warrant and covenant that they will offer and sell securities throughout the applicable distribution compliance period exclusively in compliance with either Regulation S or any other available exemption from the Securities Act registration requirements, or pursuant to a registration statement filed with the SEC. If the transaction is an equity offering by a U.S. issuer, the distributor also must agree not to engage in any hedging transactions involving Category 2 or Category 3 securities during the distribution compliance period, unless in compliance with the Securities Act.

If there is a standalone Regulation S offering (or the combined offering is structured to permit separate Rule 144A and Regulation S syndicates), the agreement between the financial intermediaries and the issuer may
be very dissimilar to a U.S. style purchase (or underwriting) agreement.

5. **Indenture and the Trust Indenture Act.**

Because Rule 144A and Regulation S debt offerings are exempt from the registration requirements of the Securities Act, the indenture will not need to be qualified under the Trust Indenture Act of 1939, as amended (the “Trust Indenture Act”). However, these debt offerings, particularly of U.S. issuers contemplating a subsequent registered exchange offering, should be issued under an indenture that is qualifiable under the Trust Indenture Act. When the registration statement is subsequently filed, the indenture must then be qualified under the Trust Indenture Act. In the ordinary course, issuers and initial purchasers choose trustees that can comply with the requirements of the Trust Indenture Act, but such trustee qualification (on Form T-1) also is required when the registration statement is subsequently filed. Although it is standard to use an indenture, if the debt will not be registered subsequently with the SEC (which usually is the case in a standalone Regulation S offering), a fiscal and paying agency agreement may be used that covers substantially the same matters.

**What is the due diligence process for initial purchasers in connection with a Regulation S offering?**

While it is generally believed that Rule 144A and Regulation S offerings are not subject to the liability provisions of Section 11 or Section 12(a)(2) of the Securities Act, thereby limiting the potential need to establish a formal “due diligence” defense, the issuer and the initial purchasers could, under some circumstances, be subject to liability for rescission under Section 12(a)(1), as well as be subject to private rights of action under Section 10(b) of the Exchange Act and Rule 10b-5 for material misstatements or omissions. Thus, a thorough due diligence investigation by the initial purchasers and their counsel generally will result in better disclosure and a lower risk of liability or potential liability for material misstatements or omissions, satisfy the initial purchasers’ internal risk management requirements and protect their institutional reputations.

In a predominately Regulation S offering with a small Rule 144A tranche, non-U.S. offering participants may proceed with less diligence. However, if an initial purchaser is committing to purchase all the securities and is requiring negative assurance letters from counsel, this seems unlikely. Limited due diligence, therefore, is more likely in standalone Regulation S offerings that do not involve firm commitments from the financial intermediaries.

The due diligence process can be divided into two parts: (1) financial, business and management due diligence, and (2) documentary, or legal, due diligence. The actual extent of diligence required may vary based on:

- the nature of the issuer, including whether the issuer is a newer entity, a well-established company (whether public or not) or a U.S. reporting company;
- the business of the issuer and its current risk profile; and
- the securities to be offered, whether investment grade or high yield debt securities (and the ratings, if any, of similar securities of the issuer) or preferred or common equity.

An issuer, its investment banks and their respective counsel may negotiate the expected extent of the
For example, in a large high yield debt offering, the extent of the due diligence will mirror that of a public offering.

In order to help establish a due diligence defense, market practice requires the initial purchasers in Rule 144A and Regulation S offerings to condition the offerings upon receipt of documents similar to those used in an underwritten offering, including a comfort letter, legal opinions and officer certificates, as discussed above.

**Liability Issues**

Failure to comply with the conditions of Regulation S may trigger liability under certain provisions of the Securities Act, the Exchange Act, and applicable state blue sky laws.

**Does the failure to comply with the conditions of Regulation S trigger Securities Act liability?**

1. **Section 12 Liability**

   Section 12 of the Securities Act imposes liability on any person who offers or sells a security in violation of Section 5 or by means of a prospectus or oral communication that includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in light of the circumstances under which they were made, not misleading. Section 12 does not require reliance on the misstatement or omission, or even the receipt of a prospectus. Liability under Section 12 may be for rescission, if the security is still owned by the defendant, or for damages, if the security is no longer owned by the defendant. A defense may be sustained under Section 12(a)(2) if the person selling the security can demonstrate that “he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission.” Despite the fact that the statute does not explicitly require the defendant to actually exercise reasonable care, the “reasonable care” standard under Section 12(a)(2) appears to be the same as the Section 11 “reasonable investigation” standard for the “due diligence” defense. Therefore, the defendant must establish that it performed due diligence in order to sustain the defense.

   The U.S. Supreme Court has ruled that the term “prospectus” for purposes of Section 12(a)(2) has the same meaning as it does under Section 10. Since the prospectus requirements under Section 10 are only triggered if an offering is required to be registered under Section 5, transactions exempt from the registration requirements of Section 5 pursuant to Section 4 are not subject to the liability provisions of Section 12(a)(2). As a result, private placements of securities that are exempt from the registration requirements of Section 5 pursuant to Section 4, as well as Rule 144A and Regulation S offerings, are not subject to Section 12(a)(2) liability. However, an offering made in reliance on Regulation S, but which fails to comply with the applicable Regulation S safe harbors, may still be subject to the liability provisions of Section 12(a)(2).

2. **Section 11 Liability**

   Under Section 11 of the Securities Act, liability may arise from misstatements or omissions in a registration statement at the time it became effective. However, since Regulation S provides an exclusion from the

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4 See Sanders v. John Nuveen & Co., 619 F.2d 1222 (7th Cir. 1980).
registration requirements of Section 5, Regulation S offerings do not subject the issuer and initial purchasers to liability under Section 11. Accordingly, the initial purchasers are not entitled to the “due diligence” defense that may be established under Section 11. However, underwriters often choose to conduct due diligence comparable to that conducted for a registered offering, particularly if the offering is a combined Rule 144A/Regulation S offering.

Does failure to comply with the conditions of Regulation S trigger Exchange Act liability?
Regulation S does not shield a transaction from the extraterritorial application of antifraud provisions or limit compliance with Exchange Act registration requirements or broker-dealer registration requirements.

Does failure to comply with the conditions of Regulation S trigger liability under State Blue Sky Laws?
Preliminary Note 4 to Regulation S expressly states that Regulation S does not provide a safe harbor from any applicable state blue sky laws. Many state securities laws are based on Section 414 of the Uniform Securities Act, which asserts that state jurisdiction over transactions encompasses those made in the state, including transactions in which the offer originates from the state. State securities laws are particularly likely to apply to Regulation S offerings by U.S. issuers. Many state securities laws also contain a civil liability provision substantially similar to Section 12 of the Securities Act. As a result, Regulation S transaction documents often contain, in the representations and warranties section, an acknowledgement by the issuer that the securities are exempt from or not subject to the registration requirements of any state blue sky laws.

Miscellaneous Issues

Are FINRA filing requirements applicable to Regulation S transactions?
No. Regulation S offerings are beyond the scope of FINRA filing requirements and rules governing conflicts of interests.

May an issuer publish a notice about a proposed Regulation S transaction?
Placing an advertisement containing a reference to a Regulation S offering in a publication with general circulation in the United States falls squarely within the meaning of “directed selling efforts.” A publication of “general circulation” in the United States includes any publication printed primarily for distribution in the United States or that has had on average, a circulation of at least 15,000 copies per issue, within the prior 12 months. Certain types of advertising are excluded from the definition of “directed selling efforts,” including tombstone advertisements.

May issuers use a Rule 135c-compliant press release to announce a Regulation S offering?
Yes, issuers may use a Rule 135c-compliant press release to announce a Regulation S offering. Under Rule 135c of the Securities Act, an announcement that an issuer proposes to make, is making or has made an unregistered offering will not be deemed to be an offer of securities, for purposes of Section 5 of the Securities Act, if, among other things, the announcement contains certain limited information regarding the offering (e.g.,
the name of the issuer, the basic terms and size of the offering, the timing of the offering, a brief statement of the manner and purpose of the offering and statements that the securities have not been registered) and is not used for the purpose of conditioning the market in the United States for the offered securities. A Rule 135c-compliant press release is not a "directed selling effort" and therefore will not affect the availability of the Regulation S safe harbor.

In addition, for Regulation S offerings with a Rule 144A tranche, the SEC has clarified that general solicitation and general advertising in connection with a Rule 144A offering will not be viewed as "directed selling efforts" in connection with a concurrent Regulation S offering. This is particularly relevant because general solicitation and general advertising are now permitted for Rule 144A offerings (so long as the securities are sold to a QIB or to a purchaser that the seller and any person acting on the seller’s behalf reasonably believes is a QIB). As a result, issuers As a result, issuers are now permitted to broadly disseminate a press release regarding a proposed or completed Rule 144A offering free of the prior restrictions on the types of permitted information under Rule 135c.

Offering participants should keep in mind that Rule 135c is a non-exclusive safe harbor, and offering-related press releases may be able to satisfy a different safe harbor, such as Rule 135e under the Securities Act in respect of any offshore activities for any Regulation S tranche. Under Rule 135e, foreign issuers, selling security holders or their representatives will not be deemed to offer any security for sale, for purposes of Section 5 of the Securities Act, by virtue of providing any journalist with access to any of the following:

- its press conferences held outside of the United States;
- meetings with the issuer or selling security holder representatives conducted outside of the United States; or
- written press-related materials released outside the United States, at or in which a present or proposed offering of securities is discussed, if:
  - the present or proposed offering is not being, or to be, conducted solely in the United States;
  - access is provided to both U.S. and foreign journalists;
  - and any written press-related materials pertaining to transactions in which any of the securities will be or are being offered in the United States satisfy the requirements of Rule 135e(b) with respect to legends and certain other information.

Why are Regulation S offerings sometimes considered “backdoor IPOs”?

Rule 144A and Regulation S may be used by non-reporting issuers, both domestic and foreign, for common stock offerings that sometimes are referred to as “backdoor IPOs.” However, a backdoor IPO would not be available to a foreign issuer that has either its ordinary shares or ADRs for its ordinary shares listed on a securities exchange or quoted because the ordinary shares and ADRs are considered to be of the same class and fungible within the meaning of Rule 144(d)(3)(i). The benefits of a Rule 144A/Regulation S common stock offering compared to a registered offering include:
• more flexible disclosure requirements;
• no liability for a registration statement under Section 5 of the Securities Act (although the anti-fraud provisions are still applicable);
• lower costs;
• limited ongoing reporting obligations; and
• none of the corporate governance provisions of the federal securities laws and the exchanges and related liabilities, particularly those of Sarbanes-Oxley Act.

However, one perceived drawback of a Rule 144A/Regulation S offering is the ability of the secondary Rule 144A/Regulation S trading market to absorb a large volume of equity securities. Historically, the valuation discount because of this lack of liquidity was not sufficiently offset by the benefits of the Rule 144A/Regulation S offering and the public company costs avoided. In addition, a non-reporting issuer that intends to rely on Rule 144A/Regulation S for offerings of its equity securities must monitor the number of its equity holders in order not to exceed the shareholder threshold of Section 12(g) of the Exchange Act and related rules recently amended by Titles V and VI of the Jumpstart Our Business Startups (JOBS) Act enacted on April 5, 2012. Title V amends Section 12(g)(1)(A) of the Exchange Act and provides that an issuer will become subject to Exchange Act requirements: within 120 days after the last day of its first fiscal year ended on which the issuer has total assets in excess of $10 million and a class of equity security (other than an exempted security) held of record by 2,000 or more persons.

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